

Supreme Court of the State of Virginia

VIRGINIA STATE CORPORATION OF LYNCH  
V. THE STATE

GUY T. HOLVERING COMMISSIONER OF INTER-  
NAL REVENUE

ON WRIT OF HABEAS CORPUS OF THE UNITED STATES CIRCUIT COURT  
OF APPEALS FOR THE FOURTH CIRCUIT

ENTERED FOR RECORD FEBRUARY 21, 1942

RECEIVED CLERK OF SUPREME COURT APRIL 2, 1942

# SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

No.

VIRGINIAN HOTEL CORPORATION OF LYNCH-  
BURG, PETITIONER,

*vs.*

GUY T. HELVFRING, COMMISSIONER OF  
INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES  
CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

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[fol. 1]

**BEFORE UNITED STATES BOARD OF TAX APPEALS**

Docket No. 105828

VIRGINIAN HOTEL CORPORATION OF LYNCHBURG, Petitioner,

v.

COMMIESIONER OF INTERNAL REVENUE, Respondent

**Appearances:**

For Taxpayer: O. H. Tufts, C. P. A.

For Comm'r: E. L. Corbin, Esq.

**DOCKET ENTRIES**

1940

Dec. 10. Petition received and filed. Taxpayer notified. (Fee paid).

Dec. 10. Copy of petition served on General Counsel.

1941

Jan. 30. Answer filed by General Counsel.

Jan. 30. Request for hearing in Washington, D. C., filed by General Counsel.

Feb. 3. Notice issued placing proceeding on Washington, D. C., Calendar. Answer and request served.

Sept. 18. Hearing set Nov. 10, 1941, Washington.

Nov. 10. Hearing had before Mr. Arnold on the merits. Submitted. Stipulation of facts (2) filed at hearing. Briefs due 1/10/42. Reply briefs due Jan. 24, 1942.

Nov. 24. Transcript of hearing Nov. 10, 1941, filed.

1942

Jan. 8. Brief filed by taxpayer.

Jan. 9. Motion for extension to Feb. 9, 1942 to file brief filed by General Counsel. 1/10/42 granted.

Feb. 9. Motion for extension to Mar. 11, 1942, to file brief filed by General Counsel. 2/10/42 granted.

Mar. 11. Motion for extension to March 30, 1942, to file brief filed by General Counsel. 3/12/42 granted.

Mar. 28. Brief filed by General Counsel. Served, 3/30/42.

Mar. 30. Copy of brief served on General Counsel.

Apr. 10. Reply brief filed by taxpayer. 4/11/42 copy served on General Counsel.

May 6. Memorandum opinion rendered, Arnold, Div. 12. Decision will be entered under Rule 50. 5/7/42 copy served.

May 13. Notice of settlement filed by taxpayer.

May 21. Hearing set June 10, 1942 on settlement.

May 21. Copy of notice of settlement and notice of hearing served on General Counsel.

May 25. Computation as to deficiency filed by General Counsel.

[fol. 2] May 28. Decision entered, Arnold. Div. 12.

Aug. 18. Petition for review by United States Circuit Court of Appeals, 4th Circuit, filed by General Counsel.

Aug. 25. Proof of service filed.

Aug. 26. Proof of service filed by General Counsel.

Sept. 9. Statement of points filed by General Counsel.

Sept. 9. Designation of portions of record filed by General Counsel.

Sept. 15. Proof of service of designation of record and statement of points filed by General Counsel.

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[fol. 3] BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 105828

VIRGINIAN HOTEL CORPORATION OF LYNCHBURG, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

PETITION—Filed December 10, 1940

The above-named petitioner hereby petitions for a re-determination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency issued by the Internal Revenue Agent in Charge at Richmond, Virginia, and dated September 11, 1940; and as the basis of its proceeding alleges as follows:

1. The petitioner is a corporation chartered and existing under and by virtue of the laws of the Commonwealth of Virginia, with its principal office at Church and Eighth Streets, Lynchburg, Virginia.

The return for the period here involved was filed with the Collector of Internal Revenue for the District of Virginia at Richmond, Virginia.

2. The notice of deficiency (a copy of which is hereto attached, marked Exhibit A) was mailed to the petitioner on September 11, 1940.



The said notice of deficiency refers to Internal Revenue Agent's report mailed to the petitioner of February 2, 1940; therefore, a copy of said Revenue Agent's report is hereto attached, marked Exhibit B.

3. The tax in controversy is income and excess profits tax for the calendar year ended December 31, 1938, and in the amount of \$555.26.

4. The determination of the tax set forth in said notice of deficiency is based upon the following errors:

(a). In determining the useful life of petitioner's depreciable assets to be:

|                              |           |
|------------------------------|-----------|
| Furniture and fixtures ..... | 20 Years  |
| Carpets .....                | 12½ Years |
| Cafe Improvements .....      | 20 Years  |
| Laundry Equipment .....      | 20 Years  |
| Ice Machine .....            | 20 Years  |

[fol. 4] (b). In not determining that the depreciation, computed by the petitioner and deducted on its income tax returns for the years 1931 to 1935 inclusive in excess of the allowable depreciation computed according to the respondent's rates, should be restored to the undepreciated balance of the respective assets, the said excess depreciation for the years 1931 to 1935 inclusive, aggregating \$28,262.78, not having been used to reduce taxable income on account of net losses; and in not determining that the corrected allowed depreciation for the year 1936, in excess of the corrected claimed depreciation, should be restored to the undepreciated balance of the assets, the said excess depreciation for the year 1936 in the amount of \$3,137.47 not having been used to reduce taxable income on account of the corrected net loss for said year.

(c). In determining petitioner's total allowable depreciation for the year 1938 to be \$1,295.47 instead of \$4,341.97 as determined and claimed as a deduction by the petitioner.

(d). In not determining that the petitioner had made a reasonably accurate determination of the useful life of its respective assets and that the resultant depreciation for the year 1938 was an allowable deduction from gross income.

(e). In not determining that \$70.00 capital stock tax paid for the year ended June 30, 1938, in excess of the amount of the said tax accruable at December 31, 1937, was a proper deduction from gross income for the calendar year 1938.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a). The petitioner operates the Virginian Hotel in Lynchburg, Virginia, as lessee. It owns the furniture and equipment in said hotel but does not have any interest in the hotel property and permanent fixtures.

This hotel was operated by other lessees until June 1, 1927, at which time A. F. Young and his wife, Mrs. R. E. Young, took over the unexpired lease. The Youngs operated as a partnership until December 31, 1931, when the partnership was incorporated as the petitioner herein, and all of the issued capital stock was given to the Youngs, with the exception of qualifying shares, for the net book value or cost of the assets to the partnership; the said stock having been issued in the ratio of their respective interests in the partnership.

(b). When the Youngs took over the unexpired lease of the hotel on June 1, 1927, it was completely furnished and equipped, the furniture and fixtures therein being the property of the prior lessee.

In order to avoid any interruption in the operation of the hotel, the Youngs purchased from the prior lessee all of the furniture and equipment therein for a lump sum of \$70,899.94, which amount was allocated to the respective assets in the ratio of the undepreciated balance of the same items on the vendor's ledger.

[fol. 5] (c). The total amount expended for the original purchase of the furniture and equipment of the hotel and subsequent renewals to December 31, 1938, are as follows:

| Purchased from prior Lessee June 1, 1927..... |  | Furniture<br>and Fixtures | Carpets     | Cafe<br>Improvements | Laundry<br>Equipment | Ice<br>Machine | Total        |
|---|--|---------------------------|-------------|----------------------|----------------------|----------------|--------------|
| Additions 1927.....                           |  | \$1,730.33                | \$1,247.90  | \$9,599.67           | \$.....              | \$.....        | \$12,584.90  |
| 1928.....                                     |  | 3,087.23                  | 2,745.58    | 3,894.13             | 175.00               | 121.51         | 10,023.45    |
| 1929.....                                     |  | 692.35                    | 2,395.99    | 659.08               | .....                | 325.00         | 4,072.42     |
| 1930.....                                     |  | 1,789.54                  | .....       | 214.81               | .....                | .....          | 1,997.35     |
| 1931.....                                     |  | 15,033.55                 | 4,406.74    | 3,057.04             | 1,011.23             | 241.65         | 23,750.21    |
| 1932.....                                     |  | 2,733.92                  | .....       | 242.05               | 2,447.35             | 33.68          | 5,457.00     |
| 1933.....                                     |  | .....                     | .....       | .....                | .....                | 102.96         | 102.96       |
| 1934.....                                     |  | 999.63                    | .....       | 49.86                | .....                | .....          | 1,049.49     |
| 1935.....                                     |  | 184.57                    | 814.36      | .....                | .....                | .....          | 998.93       |
| 1936.....                                     |  | 134.76                    | 686.73      | 100.00               | .....                | 75.00          | 996.49       |
| 1937.....                                     |  | 544.85                    | 622.54      | .....                | .....                | .....          | 1,167.39     |
| 1938.....                                     |  | 3,075.76                  | 2,437.79    | 915.97               | .....                | 268.44         | 6,697.96     |
| Total Additions.....                          |  | \$30,006.49               | \$15,357.63 | \$18,732.61          | \$3,633.58           | \$1,168.24     | \$68,898.55  |
| Grand Totals.....                             |  | \$68,406.69               | \$34,699.33 | \$25,965.01          | \$7,736.79           | \$2,900.67     | \$139,798.49 |

(d). It was determined that the average useful life of the respective items of furniture and equipment would be:

|                        |                       |
|------------------------|-----------------------|
| Furniture and Fixtures | 10 Years              |
| Carpets                | 6 $\frac{2}{3}$ Years |
| Cafe Improvements      | 10 Years              |
| Laundry Equipment      | 10 Years              |
| Ice Machine            | 10 Years              |

and depreciation has been charged off each year on this basis, allowance having been made for any items which became fully depreciated.

(e). The total depreciation charged off and claimed as a deduction from gross income for the year 1938 was \$4,341.97.

(f). In 1940, the respondent determined that the average useful life of the respective items from the time of acquisition was:

|  |                        |
|--|------------------------|
| Furniture and Fixtures                             | 20 Years               |
| Carpets  | 12 $\frac{1}{2}$ Years |
| [fol. 6] Cafe Equipment                            | 20 Years               |
| Laundry Equipment                                  | 20 Years               |
| Ice Machine  | 20 Years               |
| Air Conditioning Equipment<br>(a new item in 1938) | 20 Years               |

and computed the allowable depreciation for the year 1938, as set forth in detail on pages 6 and 7 of Exhibit B, to be \$1,295.47.

(g). The respondent having determined that the 20 and 12 $\frac{1}{2}$  year useful life of the respective items was applicable from the time of their acquisition, depreciation for the prior years should be re-computed as set forth in detail in Exhibit C, annexed hereto and made a part of this petition.

(h). The difference between the depreciation computed according to the petitioner's rates for the years 1931 to 1935 inclusive, and the depreciation allowable according to the respondent's rates for the said period, was not used to reduce taxable income; therefore, this excess in the sum of \$28, 262. 78 should be restored to the undepreciated cost of the assets at December 31, 1937. Excess deprecia-

tion in the amount of \$3,137.47, deducted for the year 1936, should also be restored to the undepreciated balance of the assets at December 31, 1937. This amount is computed as follows:

|   | Deprec.<br>Deducted<br>Return | Net Loss<br>Return |
|---|-------------------------------|--------------------|
| Original.....   | \$10,982.50                   | \$1,663.95         |
| Add: Depreciation allowable on carpets. \$2,398.08<br>deducted..... 924.56      |                               |                    |
| Additional allowable resulting from decrease of<br>allowable for 1931-1935..... | 1,473.52                      | 1,473.52           |
| Corrected.....  | \$12,456.02                   | \$3,137.47         |
| Corrected income return loss.....   | 3,137.47                      |                    |
| Total depreciation allowed.....   | \$9,318.55                    |                    |
| Less: Minimum allowable:  |                               |                    |
| Carpets..... \$2,398.08   |                               |                    |
| Truck..... 37.50  | 2,435.58                      |                    |
| Balance depreciation allowed..... (1) \$6,882.97                                |                               |                    |

(1) Applicable to Furniture and Fixtures, Improvements to Cafe, Laundry Machinery and Ice Machine, or 68.6892% of \$10,020.44 deducted for these items.

[fol. 7] (i). The petitioner accrued at December 31, 1937, and deducted from gross income on its income tax return for the calendar year 1937, a capital stock tax of \$55.00, payable July, 1938, computed according to the provisions of Section 105 of the Revenue Act of 1935 as amended by Section 401 of the Revenue Act of 1936, as follows:

|   |                    |
|---|--------------------|
| Adjusted Declared Value, June 30, 1937—Form 707 ..... | \$48,336.05        |
| Additions:  |                    |
| Net Income for Year 1937.....                         | 7,235.91           |
|   | <u>\$55,571.96</u> |
| Deductions:   | None               |
| Adjusted Declared Value, June 30, 1938.....           | <u>\$55,571.96</u> |
| Tax at \$1.00 for each \$1,000.00.....                | \$ 55.00           |

(j). Section 601 (f)(1) of the Revenue Act of 1938, effective May 28, 1938, gave taxpayers the right to declare a new value for the Capital Stock Tax year ended June 30, 1938, instead of using the adjusted declared value as required by the Revenue Act of 1935 as amended. Ac-

cordingly, the petitioner declared a value of \$125,000.00 and paid a tax of \$125.00, or \$70.00 more than the amount accruable at December 31, 1937. The right to accrue and deduct the additional \$70.00 Capital-Stock Tax did not exist prior to the enactment of the Revenue Act of 1938, or May 28, 1938.

6. Wherefore, the petitioner prays that this Board may hear the proceeding and determine:

(a). That the petitioner has correctly determined the average life of its depreciable assets and that the aggregate depreciation claimed as a deduction on its income return for the year 1938, in the amount of \$4,341.97, is allowable.

(b). That if the Board determines that the average useful life of the respective assets, as determined by the respondent, should have been used, then, in that event, the allowable depreciation for the years 1931 to 1936 should be recomputed, using respondent's rates, and the excess depreciation deducted by the petitioner, aggregating \$31,400.25, should be restored to the undepreciated balance of the assets at December 31, 1937; and that the allowable depreciation for the year 1938 is \$4,438.14, as set forth in detail in Exhibit B, annexed hereto and made a part of this petition.

(c). That the \$70.00 Capital-Stock Tax paid for the year ended June 30, 1938, over and above the amount accrued and deducted by the petitioner at December 31, 1937, was not accruable prior to the effective date of the Revenue Act of 1938, or May 28, 1938, and that said \$70.00 is a proper deduction from gross income for the year 1938.

O. H. Tufts, Agent for Petitioner, 512 Krise Building, Lynchburg, Virginia.

[fol. 8] *Duly sworn to by A. F. Young jurat omitted in printing.*



[fol. 9]

## EXHIBIT "A" TO PETITION

## Treasury Department

## Internal Revenue Service

Richmond, Virginia,  
Sept. 11, 1940.

Virginian Hotel Corporation of Lynchburg, Church & 8th  
Streets, Lynchburg, Virginia.

## GENTLEMEN :

You are advised that the determination of your income tax liability for the taxable year(s) ended Dec. 31, 1938 discloses a deficiency of \$416.94 and that the determination of your excess-profits tax liability for the year(s) mentioned discloses a deficiency of \$138.32 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiencies mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Richmond, Virginia for the attention of IT:Rec. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully, Guy T. Helvering, Commissioner, by  
S. R. Brame, Internal Revenue Agent in Charge.

Enclosures: Statement. Form of waiver.

ES.

[fol. 10]

## Statement

Virginian Hotel Corporation of Lynchburg,  
Church and 8th Streets,  
Lynchburg, Virginia

Tax liability for taxable year ended December 31, 1938.

Income Tax

| Liability  | Assessed   | Deficiency |
|------------|------------|------------|
| \$1,978.39 | \$1,561.45 | \$416.94   |

Excess-Profits Tax

|          |        |          |
|----------|--------|----------|
| \$138.32 | \$0.00 | \$138.32 |
|----------|--------|----------|

In making this determination of your income tax and excess-profits tax liability, careful consideration has been given to the internal revenue agent's report dated January 31, 1940, copy of which was mailed to you February 2, 1940; to your protest dated April 30, 1940; to statements made at conference held in office of Internal Revenue Agent in Charge at Richmond, Virginia, on June 4, 1940; to letter from your accountant dated July 22, 1940 and to statements made at conference held before Technical Staff, Atlantic Division at Richmond, Virginia, on July 17, 1940.

A copy of this letter and statement has been mailed to your representative, Mr. O. H. Tufts, C. P. A., Lynchburg, Virginia, in accordance with the authority contained in the power of attorney executed by you and on file with the Bureau.

Adjustments to Net Income—1938

|   |             |
|---|-------------|
| Net income as disclosed by return .....       | \$11,688.90 |
| Unallowable deductions and additional income: |             |
| (a) Depreciation .....                        | 3,046.50    |
| (b) Capital stock tax .....                   | 70.00       |
|   | <hr/>       |
| Net income adjusted .....                     | \$14,805.40 |

[fol. 11]

## Explanation of Adjustments

(a) Your contention that the accumulated depreciation reserve at December 31, 1937, should not include the excess depreciation of prior years which did not reduce taxable income is denied.

Computation of excessive depreciation disallowed is as follows:

| Rate | Assets                      | Cost              | Depreciation<br>Reserve<br>12/31/37 | Depreciation<br>1938 |
|------|-----------------------------|-------------------|-------------------------------------|----------------------|
| 5%   | Furniture & Fixtures....    | \$68,406.69       | \$56,722.75                         | \$690.47             |
| 8%   | Carpets.....                | 34,699.33         | 30,534.33                           | 263.14               |
| 5%   | Air Conditioning Equip. .   | 2,612.67          | .....                               | 65.34                |
| 5%   | Cafe Equipment.....         | 25,966.61         | 23,407.03                           | 147.67               |
| 15%  | Laundry Equipment.....      | 7,736.79          | 6,273.80                            | 102.91               |
| 5%   | Ice Plant.....              | 2,990.67          | 2,447.32                            | 25.94                |
|      |                             | <u>142,412.76</u> | <u>119,385.23</u>                   | <u>1,295.47</u>      |
|      | Depreciation claimed.....   |                   |                                     | 4,341.97             |
|      | Excessive depreciation..... |                   |                                     | <u>3,046.50</u>      |

(b) Your contention that additional capital stock tax for the year ended June 30, 1938 which accrued 7/1/37 but was paid in 1938 should be allowed as a deduction in that year is not allowed.

### Computation of Tax

#### Excess-Profits Tax Computation

|  |               |
|--|---------------|
| Value of capital stock as declared in the capital stock tax return for year ended 6/30/38..... | \$125,000.00  |
| Net income for excess-profits tax computation ..   | 14,805.40     |
| Less: Dividends received credit .....  | .....         |
| Balance of net income .....  | 14,805.40     |
| Less: 10% of capital stock declared value .....  | 12,500.00     |
| Net income subject to excess-profits tax .....   | 2,305.40      |
| Amount taxable at 6% .....   | 2,305.40      |
| Excess-profits tax at 6% .....   | 138.32        |
| Total excess-profits tax .....   | 138.32        |
| Tax previously assessed, original, account #410528 .....                                       | 0.00          |
| Additional tax to be assessed .....  | <u>138.32</u> |

### Income Tax Computation

|   |           |
|---|-----------|
| Net income for excess-profits computation .....             | 14,805.40 |
| Less: Excess-profits tax .....                              | 138.32    |
| Net income .....  | 14,667.08 |
| Special class net income .....                              | 14,667.08 |
| Portion taxable at 12½%—\$5,000.00 .....                    | 625.00    |
| Portion taxable at 14% 9,667.08 .....                       | 1,353.39  |
| Total .....   | 1,978.39  |
| Tax previously assessed, original, account<br>#410528 ..... | 1,561.45  |
| Additional tax to be assessed .....                         | 416.94    |

[fol. 12]

### EXHIBIT "B" TO PETITION

Treasury Department

Internal Revenue Service

Office of Internal Revenue Agent in Charge

Virginia Division

Richmond, Virginia,  
February 2, 1940.

Virginian Hotel Corp. of Lynchburg, Church and Eighth  
Street, Lynchburg, Virginia.

GENTLEMEN :

I enclose a copy of the report of the examination of your income-tax returns for the years shown below. After consideration by this office, the following adjustment of your tax liability appears to be warranted, for the reasons stated in the report:

| Year                  | Additional Tax |                    |
|-----------------------|----------------|--------------------|
|                       | Income Tax     | Excess Profits Tax |
| 1938 .....            | \$416.10       | \$144.32           |
| Total Additional Tax: | \$560.42       |                    |

*If you agree to this adjustment, the enclosed form of waiver should be executed and forwarded to this office promptly, in order to permit the early assessment of the additional tax and to stop the accumulation of interest. Such interest will cease 30 days after the receipt of the executed form, or upon the payment of the additional tax to the collector, whichever occurs first.*

*If you desire to make immediate payment of the additional tax without awaiting assessment, you should forward your remittance to the Collector of Internal Revenue at Richmond, Virginia, enclosing this letter, or a copy thereof. Interest on the additional tax should be included in your remittance, computed at the rate of 6 percent per annum from the due date of the first installment to the date of payment.*

*If you do not agree to the proposed adjustment, you may file a protest, executed in triplicate under oath, with this office, within 30 days from the date of this letter, stating the grounds for your exceptions. Any protest so filed will have careful consideration, and, if you so request, an opportunity for a hearing in this office will be granted you prior to final determination of any deficiency against you. This letter is not a final notice of deficiency, and this office will be pleased to answer any questions which may occur to you in your examination of the enclosed copy of the report.*

*Should you fail to pay the additional tax to the collector of internal revenue or to file with this office within the 30-day period mentioned either a waiver on the enclosed form or a written protest, final determination of your tax liability will be made and a notice of deficiency will be sent you in accordance with the provisions of law applicable to the assessment and collection of income- and excess-profits-tax deficiencies.*

*Your prompt acknowledgment of the receipt of this letter and related papers upon the enclosed form will be much appreciated.*

*(Signed) S. R. Brame, Internal Revenue Agent in Charge.*

*Enclosures: Report of examination. Form of waiver. Form of acknowledgment. Form 744.*

MWM/iog.

## [fol. 13] Virginian Hotel Corporation of Lynchburg

## Table of Contents:

## Preliminary Statement Schedules 1 and 2, Exhibit A

## Preliminary Statement

| Year | Deficiency in<br>Excess Profits Tax | Deficiency in<br>Income Tax |
|------|-------------------------------------|-----------------------------|
| 1938 | \$144.32                            | \$416.10                    |

Gross income and deductions from gross income were verified.

## Depreciation

This hotel was opened in 1913. The present operators purchased the equipment as of June 1, 1917. A review of the ledger accounts discloses that expenditures for replacements, have been relatively small in amounts and that the greater part of the additions to the equipment accounts, were for betterments and additional equipment. A large addition to the hotel building was made in 1931. It is apparent that the rate of 10% is excessive and that the equipment has an average life of approximately twenty years.

Mr. A. F. Young and wife operated this hotel as a partnership from June 1, 1927 to 1930. It was incorporated in 1930 and has since been operated as a corporation. Values of the assets remained unchanged after the incorporation since no change in actual ownership was involved.

The deficit of \$56,020.25 was created by large operating losses during the years 1931 to 1936, inclusive.

The adjustments have not been agreed to. Mr. O. H. Tufts, C. P. A., disagrees with the adjustments.

## [fol. 14] Virginia Hotel Corporation of Lynchburg,

## Schedule 1—Year Ended Dec. 31, 1938

## Adjustments to Net Income

|   |             |
|---|-------------|
| Net income as disclosed by return ..... | \$11,688.90 |
| As corrected .....                      | 14,805.40   |
| Net adjustment as computed below .....  | 3,116.50    |



## Unallowable deductions and additional income:

|                               |            |          |
|-------------------------------|------------|----------|
| (a) Depreciation .....        | \$3,046.50 |          |
| (b) Capital stock tax .....   | 70.00      |          |
| Total .....                   |            | 3,116.50 |
| Net adjustment as above ..... |            | 3,116.50 |

## Schedule 1-A

## Explanation of Items

|                             |          |
|-----------------------------|----------|
| (a) Depreciation .....      | 3,046.50 |
| See Exhibit A               |          |
| (b) Capital stock tax ..... | 70.00    |

Capital stock tax paid for the fiscal year ended June 30, 1938. This tax accrued on July 1, 1937.

Note: Agent's computation of taxes, Schedule 2—pages 3 and 4, omitted from copy.

[fol. 15]

## Virginian Hotel Corporation of Lynchburg

|                             | Reserve<br>12-31-37 | Depreciation<br>allowable | Reserve<br>12-31-38 |
|-----------------------------|---------------------|---------------------------|---------------------|
| Furn. & Fixtures.....       | 56,722.75           | 690.47                    | 57,413.22           |
| Carpets.....                | 30,534.33           | 263.14                    | 30,797.47           |
| Air Conditioning Equip..... |                     | 65.34                     | 65.34               |
| Cafe Equipment.....         | 23,407.03           | 147.67                    | 23,554.70           |
| Laundry Equipment.....      | 6,273.80            | 102.91                    | 6,376.71            |
| Ice Plant.....              | 2,447.32            | 25.94                     | 2,473.26            |
|                             | <u>119,385.23</u>   | <u>1,295.47</u>           | <u>120,680.70</u>   |
| Depreciation claimed.....   |                     | 4,341.97                  |                     |
| Depreciation allowable..... |                     | <u>1,295.47</u>           |                     |
|                             |                     | 3,046.50                  |                     |

[fol. 16]

Depreciation  
Virginia Hotel Corporation of Lynchburg—Exhibit B—Contd.

| Furn. & Fix. | Year in Which Purchased | Totals    | Additions | Reserve 12-31-37 | Balance   | Estimate of Life | Years in Service | Beginning Life | Depreciation 1938 |
|--------------|-------------------------|-----------|-----------|------------------|-----------|------------------|------------------|----------------|-------------------|
|              | 1913 to                 |           |           |                  |           |                  |                  |                |                   |
|              | 6-1-27                  | (a)       | 38,400.20 | 38,400.20        | .....     | 20 yr.           | 10½ to 24        | 9½             | None              |
|              | 1927                    | .....     | 1,730.33  | 1,730.33         | .....     | 20 yr.           | 10½              | 10½            | None              |
|              | 1928                    | .....     | 3,087.23  | 2,932.84         | 154.39    | "                | 9½               | 10½            | 14.70             |
|              | 1929                    | .....     | 692.35    | 588.54           | 103.81    | "                | 8½               | 11½            | 9.02              |
|              | 1930                    | .....     | 1,789.54  | 1,342.12         | 447.42    | "                | 7½               | 12½            | 35.79             |
|              | 1931                    | .....     | 15,033.55 | 9,771.83         | 5,261.72  | "                | 6½               | 13½            | 389.76            |
|              | 1932                    | .....     | 2,733.92  | 1,503.64         | 1,230.28  | "                | 5½               | 14½            | 84.85             |
|              | 1934                    | .....     | 999.63    | 349.89           | 649.74    | "                | 3½               | 16½            | 39.38             |
|              | 1935                    | .....     | 184.57    | 55.90            | 128.67    | "                | 2½               | 17½            | 7.35              |
|              | 1936                    | .....     | 134.76    | 20.22            | 114.54    | "                | 1½               | 18½            | 6.19              |
|              | 1937                    | 65,330.93 | 544.85    | 27.24            | 517.61    | "                | ½                | 19½            | 26.54             |
|              | 1938                    | 68,406.69 | 3,075.76  | .....            | 3,075.76  | "                | .....            | 20             | 76.89             |
|              |                         |           |           | 56,722.75        | 11,683.94 |                  |                  |                | 690.47            |
| Carpets      | 1913 to                 |           |           |                  |           |                  |                  |                |                   |
|              | 6-1-27                  | (a)       | 19,341.70 | 19,341.70        | .....     | 12½              | 10½ to 24        | 2              | .....             |
|              | 1927                    | .....     | 1,247.90  | 1,247.90         | .....     | "                | 10½              | 3              | .....             |
|              | 1928                    | .....     | 2,745.58  | 2,745.58         | .....     | "                | 8½               | 4              | .....             |
|              | 1929                    | .....     | 2,395.99  | 2,395.99         | .....     | "                | 6½               | 6              | .....             |
|              | 1931                    | .....     | 4,406.74  | 4,296.56         | 110.18    | "                | 2½               | 10             | 18.36             |
|              | 1935                    | .....     | 814.36    | 305.40           | 508.96    | "                | 1½               | 11             | 50.90             |
|              | 1936                    | .....     | 686.73    | 154.51           | 532.22    | "                | ½                | 12             | 48.38             |
|              | 1937                    | 32,261.54 | 622.54    | 46.69            | 575.85    | "                | .....            | 12½            | 47.99             |
|              | 1938                    | 34,609.33 | 2,437.70  | .....            | 2,437.79  | "                | .....            | .....          | 97.51             |
|              |                         |           |           | 30,534.33        | 4,165.00  |                  |                  |                | 263.14            |

(a) Hotel was opened in 1913. As of June 1, 1927 the present owners purchased the equipment. The original purchase of equipment, therefore, covered assets which had been put in service between 1913 and 1937.

## Air Con. Equip.

| '338 | 2,613.67 | 2,613.67 | ..... | 2,612.67 | 20 yrs. | .. | Remaining<br>20 | 65.34 |
|------|----------|----------|-------|----------|---------|----|-----------------|-------|
|      |          | 2,612.67 | ..... | 2,613.67 |         |    |                 | 65.34 |

## Cafe Equip.

| 1913 to<br>6-1-27 | .....     | 7,234.00  | 7,234.00  | None     | 20 yrs. | 10 1/2 to 24 | ..     | None   |
|-------------------|-----------|-----------|-----------|----------|---------|--------------|--------|--------|
| 1927              | .....     | 9,599.67  | 9,599.67  | None     | "       | 10 1/2       | 9 1/2  | None   |
| 1928              | .....     | 3,899.40  | 3,899.40  | 194.73   | "       | 9 1/2        | 10 1/2 | 18.55  |
| 1929              | .....     | 659.08    | 560.20    | 98.88    | "       | 8 1/2        | 11 1/2 | 8.60   |
| 1930              | .....     | 214.81    | 161.10    | 53.71    | "       | 7 1/2        | 12 1/2 | 4.30   |
| 1931              | .....     | 3,057.04  | 1,987.05  | 1,069.99 | "       | 6 1/2        | 13 1/2 | 79.26  |
| 1932              | .....     | 242.05    | 133.15    | 108.90   | "       | 5 1/2        | 14 1/2 | 7.51   |
| 1934              | .....     | 49.86     | 17.46     | 32.40    | "       | 3 1/2        | 15 1/2 | 1.96   |
| 1936              | 25,050.64 | 100.00    | 15.00     | 85.00    | "       | 1 1/2        | 18 1/2 | 4.59   |
| 1938              | 25,966.61 | 915.97    | .....     | 915.97   | "       | ..           | 20     | 22.90  |
|                   |           | 25,966.61 | 23,407.03 | 2,559.58 |         |              |        | 147.67 |

## Laundry Equip.

|      |          |          |          |          |         |     |     |         |
|------|----------|----------|----------|----------|---------|-----|-----|---------|
| 1927 | .....    | 4,103.21 | 4,103.21 | None     | 20 yrs. | 10½ | 10½ | .....74 |
| 1928 | .....    | 175.00   | 167.25   | 7.75     | "       | 9½  | 10½ | 26.22   |
| 1931 | .....    | 1,011.23 | 657.28   | 353.95   | "       | 6½  | 13½ | 75.95   |
| 1932 | 7,736.79 | 2,447.35 | 1,346.06 | 1,101.29 | "       | 5½  | 14½ |         |
|      |          | 7,736.79 | 6,273.80 | 1,462.99 |         |     |     | 102.91  |

## Ice Plant

|      |          |          |          |        |         |        |        |         |
|------|----------|----------|----------|--------|---------|--------|--------|---------|
| 1927 | .....    | 1,822.43 | 1,822.43 | .....  | 20 yrs. | 10 1/2 | 9 1/2  | .....58 |
| 1928 | .....    | 121.51   | 115.42   | 6.09   | "       | 9 1/2  | 10 1/2 | ..58    |
| 1929 | .....    | 325.00   | 276.25   | 48.75  | "       | 8 1/2  | 11 1/2 | 4.24    |
| 1931 | .....    | 241.65   | 157.09   | 84.56  | "       | 6 1/2  | 13 1/2 | 6.26    |
| 1932 | .....    | 33.68    | 18.53    | 15.15  | "       | 5 1/2  | 14 1/2 | 1.04    |
| 1933 | .....    | 122.96   | 46.35    | 56.61  | "       | 4 1/2  | 15 1/2 | 3.65    |
| 1936 | 2,722.23 | 75.00    | 11.25    | 63.75  | "       | 1 1/2  | 18 1/2 | 3.45    |
| 1938 | 2,990.67 | 268.44   | .....    | 268.44 | "       | ..     | 20     | 6.72    |
|      |          | 2,990.67 | 2,447.32 | 543.35 |         |        |        | 25.94   |

(Here follows 1 paster, Exhibit "C", side folios 18-19)

**EXHIBIT "C" TO PETITION**  
**Virginian Hotel Corporation of Lynchburg**  
**Lynchburg, Virginia**

| Depreciation Allowed or Allowable  |      |                     |                    |                    |                   |                   |                   |                   |                   |                   |                    |
|--|------|---------------------|--------------------|--------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|--------------------|
|  |      | Asset<br>Additions  | 1927-30<br>Allowed | 1931<br>Allowable  | 1932<br>Allowable | 1933<br>Allowable | 1934<br>Allowable | 1935<br>Allowable | 1936<br>Allowed   | 1937<br>Allowed   | Total              |
| Furniture and Fixtures:  | 1927 | \$38,400.20         | \$13,440.07        | \$1,920.01         | \$1,920.01        | \$1,920.01        | \$1,920.01        | \$1,920.01        | \$2,637.68        | \$1,920.02        | \$27,597.82        |
|  | 1927 | 1,730.33            | 605.61             | 86.52              | 86.52             | 86.52             | 86.52             | 86.52             | 118.85            | 86.53             | 1,243.59           |
|  | 1928 | 3,087.23            | 771.80             | 154.36             | 154.36            | 154.36            | 154.36            | 154.36            | 212.00            | 308.72            | 2,064.38           |
|  | 1929 | 692.35              | 103.86             | 34.62              | 34.62             | 34.62             | 34.62             | 34.62             | 47.56             | 69.24             | 393.76             |
|  | 1930 | 1,789.54            | 89.47              | 89.48              | 89.48             | 89.48             | 89.48             | 89.48             | 122.92            | 178.95            | 838.74             |
|  | 1931 | 15,033.55           | .....              | 375.84             | 751.68            | 751.68            | 751.68            | 751.68            | 1,032.65          | 1,503.36          | 5,918.57           |
|  | 1932 | 2,733.92            | .....              | .....              | 68.35             | 136.70            | 136.70            | 136.70            | 187.79            | 273.39            | 939.63             |
|  | 1934 | 999.63              | .....              | .....              | .....             | .....             | 24.99             | 49.98             | 68.67             | 99.97             | 243.61             |
|  | 1935 | 184.57              | .....              | .....              | .....             | .....             | .....             | 4.61              | 17.14             | 18.46             | 40.21              |
|  | 1936 | 134.76              | .....              | .....              | .....             | .....             | .....             | .....             | 4.63              | 13.48             | 18.11              |
|  | 1937 | 544.85              | .....              | .....              | .....             | .....             | .....             | .....             | .....             | 27.24             | 27.24              |
|  |      |                     | <u>\$65,330.93</u> | <u>\$15,010.81</u> | <u>\$2,660.83</u> | <u>\$3,105.02</u> | <u>\$3,173.37</u> | <u>\$3,198.36</u> | <u>\$3,227.96</u> | <u>\$4,449.95</u> | <u>\$4,499.36</u>  |
| Carpets:   | 1927 | \$19,341.70         | \$10,154.41        | \$1,547.34         | \$1,547.34        | \$1,547.34        | \$1,547.34        | \$1,547.34        | \$1,450.59        | \$.....           | \$19,341.70        |
|  | 1927 | 1,247.90            | 657.75             | 99.83              | 99.83             | 99.83             | 99.83             | 99.83             | 91.00             | .....             | 1,247.90           |
|  | 1928 | 2,745.58            | 1,029.68           | 219.65             | 219.65            | 219.65            | 219.65            | 219.65            | 219.65            | 219.65            | 2,567.23           |
|  | 1929 | 2,395.99            | 529.10             | 191.68             | 191.68            | 191.68            | 191.68            | 191.68            | 191.68            | 191.68            | 1,870.86           |
|  | 1931 | 4,406.74            | .....              | 176.27             | 352.54            | 352.54            | 352.54            | 352.54            | 352.54            | 352.54            | 2,291.51           |
|  | 1935 | 814.36              | .....              | .....              | .....             | .....             | .....             | 32.57             | 65.15             | 65.15             | 162.87             |
|  | 1936 | 686.73              | .....              | .....              | .....             | .....             | .....             | .....             | 27.47             | 54.94             | 82.41              |
|  | 1937 | 622.54              | .....              | .....              | .....             | .....             | .....             | .....             | .....             | (1) 48.91         | 48.91              |
|  |      | <u>\$32,261.54</u>  | <u>\$12,370.94</u> | <u>\$2,234.77</u>  | <u>\$2,411.04</u> | <u>\$2,411.04</u> | <u>\$2,411.04</u> | <u>\$2,443.61</u> | <u>\$2,398.08</u> | <u>\$932.87</u>   | <u>\$27,613.39</u> |
|  |      |                     |                    |                    |                   |                   |                   |                   | (2)               |                   |                    |
| Cafe Improvements:   | 1927 | \$7,232.40          | \$2,531.34         | \$361.62           | \$361.62          | \$361.62          | \$361.62          | \$361.62          | \$496.79          | \$361.65          | \$5,197.88         |
|  | 1927 | 9,599.67            | 3,359.86           | 479.98             | 479.98            | 479.98            | 479.98            | 479.98            | 659.39            | 480.02            | 6,899.17           |
|  | 1928 | 3,894.13            | 973.53             | 194.71             | 194.71            | 194.71            | 194.71            | 194.71            | 267.48            | 389.41            | 2,602.97           |
|  | 1929 | 659.08              | 98.85              | 32.95              | 32.95             | 32.95             | 32.95             | 32.95             | 45.27             | 65.91             | 374.78             |
|  | 1930 | 214.81              | 10.74              | 10.74              | 10.74             | 10.74             | 10.74             | 10.74             | 14.75             | 21.48             | 100.67             |
|  | 1931 | 3,057.04            | .....              | 76.43              | 152.85            | 152.85            | 152.85            | 152.85            | 209.98            | 305.70            | 1,203.51           |
|  | 1932 | 242.05              | .....              | .....              | 6.05              | 12.10             | 12.10             | 12.10             | 16.63             | 24.21             | 83.19              |
|  | 1934 | 49.86               | .....              | .....              | .....             | .....             | 1.25              | 2.49              | 3.43              | 4.99              | 12.16              |
|  | 1936 | 100.00              | .....              | .....              | .....             | .....             | .....             | .....             | 3.44              | 10.00             | 13.44              |
|  |      | <u>\$25,049.04</u>  | <u>\$6,974.32</u>  | <u>\$1,156.43</u>  | <u>\$1,238.90</u> | <u>\$1,244.95</u> | <u>\$1,246.20</u> | <u>\$1,247.44</u> | <u>\$1,717.16</u> | <u>\$1,663.37</u> | <u>\$16,488.77</u> |
| (fol. 19)  |      |                     |                    |                    |                   |                   |                   |                   |                   |                   |                    |
| Laundry Equipment:   | 1927 | \$4,103.21          | \$1,436.12         | \$205.16           | \$205.16          | \$205.16          | \$205.16          | \$205.16          | \$281.85          | \$205.17          | \$2,948.94         |
|  | 1928 | 175.00              | 44.75              | 8.75               | 8.75              | 8.75              | 8.75              | 8.75              | 12.02             | 17.50             | 118.02             |
|  | 1931 | 1,011.23            | .....              | 25.28              | 50.56             | 50.56             | 50.56             | 50.56             | 69.46             | 101.12            | 398.10             |
|  | 1932 | 2,447.35            | .....              | .....              | 61.18             | 122.37            | 122.37            | 122.37            | 168.10            | 244.74            | 841.13             |
|  |      | <u>\$7,736.79</u>   | <u>\$1,480.87</u>  | <u>\$239.19</u>    | <u>\$325.65</u>   | <u>\$386.84</u>   | <u>\$386.84</u>   | <u>\$386.84</u>   | <u>\$531.43</u>   | <u>\$568.53</u>   | <u>\$4,306.19</u>  |
| Ice Machine:   | 1927 | \$1,822.43          | \$637.84           | \$91.12            | \$91.12           | \$91.12           | \$91.12           | \$91.12           | \$125.18          | \$91.15           | \$1,309.77         |
|  | 1928 | 121.51              | 30.37              | 6.08               | 6.08              | 6.08              | 6.08              | 6.08              | 8.35              | 12.15             | 81.27              |
|  | 1929 | 325.00              | 48.75              | 16.25              | 16.25             | 16.25             | 16.25             | 16.25             | 22.32             | 32.50             | 184.82             |
|  | 1931 | 241.65              | .....              | 6.04               | 12.08             | 12.08             | 12.08             | 12.08             | 16.60             | 24.17             | 95.13              |
|  | 1932 | 33.68               | .....              | .....              | .84               | 1.68              | 1.68              | 1.68              | 2.32              | 3.37              | 11.57              |
|  | 1933 | 102.96              | .....              | .....              | .....             | 2.57              | 5.15              | 5.15              | 7.08              | 10.30             | 30.25              |
|  | 1936 | 75.00               | .....              | .....              | .....             | .....             | .....             | .....             | 2.58              | 7.50              | 10.08              |
|  |      | <u>\$2,722.23</u>   | <u>\$716.96</u>    | <u>\$119.49</u>    | <u>\$126.37</u>   | <u>\$129.78</u>   | <u>\$132.36</u>   | <u>\$132.36</u>   | <u>\$184.43</u>   | <u>\$181.14</u>   | <u>\$1,722.89</u>  |
| Ford Truck:  | 1933 | \$150.00            | .....              | .....              | .....             | \$18.75           | \$37.50           | \$37.50           | \$37.50           | \$18.75           | \$150.00           |
| Grand Totals.....  |      | <u>\$133,250.53</u> | <u>\$36,553.90</u> | <u>\$6,410.71</u>  | <u>\$7,206.98</u> | <u>\$7,364.73</u> | <u>\$7,412.30</u> | <u>\$7,475.71</u> | <u>\$9,318.55</u> | <u>\$7,864.02</u> | <u>\$89,606.90</u> |
| Depreciation claimed on Income Returns.....                                |      |                     | 36,553.90          | 12,532.5           | 14,102.55         | 14,409.36         | 11,909.41         | 11,179.84         | 12,456.02         | 7,864.02          | 121,007.15         |
| Excess Depreciation Deducted and not used to<br>reduce Taxable Income..... |      |                     | \$.....            | \$6,121.34         | \$6,895.57        | \$7,044.63        | \$4,497.11        | \$3,704.13        | \$3,137.47        | \$.....           | \$31,400.25        |
| Net Losses per Returns.....  |      |                     | (Gain)             | \$8,912.97         | \$10,506.07       | \$8,879.23        | \$4,515.16        | \$6,511.52        | \$3,137.47        | (Gain)            |                    |
| (3)  |      |                     |                    |                    |                   |                   |                   |                   |                   |                   |                    |

NOTE:

|  |      |              |             |            |             |            |            |            |              |            |             |
|--|------|--------------|-------------|------------|-------------|------------|------------|------------|--------------|------------|-------------|
|  | 1937 | 544.86       |             |            |             |            |            |            |              | 27.24      | 27.24       |
|  |      | \$65,330.93  | \$15,010.81 | \$2,660.83 | \$3,105.02  | \$3,173.37 | \$3,165.36 | \$3,227.90 | \$4,449.95   | \$4,499.36 | \$39,325.66 |
| Carpets:   | 1927 | \$19,341.70  | \$10,154.41 | \$1,547.34 | \$1,547.34  | \$1,547.34 | \$1,547.34 | \$1,547.34 | \$1,450.59   | \$         | \$19,341.70 |
|  | 1927 | 1,247.90     | 657.75      | 99.83      | 99.83       | 99.83      | 99.83      | 99.83      | 91.00        |            | 1,247.90    |
|  | 1928 | 2,745.58     | 1,029.68    | 219.65     | 219.65      | 219.65     | 219.65     | 219.65     | 219.65       |            | 2,567.23    |
|  | 1929 | 2,395.99     | 529.10      | 191.68     | 191.68      | 191.68     | 191.68     | 191.68     | 191.68       |            | 1,370.86    |
|  | 1931 | 4,406.74     |             | 176.27     | 352.54      | 352.54     | 352.54     | 352.54     | 352.54       |            | 2,291.51    |
|  | 1935 | 814.36       |             |            |             |            |            | 32.57      | 65.15        |            | 162.87      |
|  | 1936 | 686.73       |             |            |             |            |            | 27.47      | 54.94        |            | 82.41       |
|  | 1937 | 622.54       |             |            |             |            |            |            | (1) 48.91    |            | 48.91       |
|  |      | \$32,261.54  | \$12,370.94 | \$2,234.77 | \$2,411.04  | \$2,411.04 | \$2,411.04 | \$2,443.61 | \$2,398.08   | \$932.87   | \$27,613.39 |
| Cafe Improvements:   | 1927 | \$7,232.40   | \$2,531.34  | \$361.62   | \$361.62    | \$361.62   | \$361.62   | \$361.62   | (2) \$496.79 | \$361.65   | \$5,197.88  |
|  | 1927 | 9,599.67     | 3,359.86    | 479.98     | 479.98      | 479.98     | 479.98     | 479.98     | 659.39       | 480.02     | 6,899.17    |
|  | 1928 | 3,894.13     | 973.53      | 194.71     | 194.71      | 194.71     | 194.71     | 194.71     | 267.48       | 389.41     | 2,603.97    |
|  | 1929 | 659.08       | 13.85       | 32.95      | 32.95       | 32.95      | 32.95      | 32.95      | 45.27        | 65.91      | 374.78      |
|  | 1930 | 214.81       | 10.74       | 10.74      | 10.74       | 10.74      | 10.74      | 10.74      | 14.75        | 21.48      | 100.67      |
|  | 1931 | 3,057.04     |             | 76.43      | 152.85      | 152.85     | 152.85     | 152.85     | 209.98       | 305.70     | 1,203.51    |
|  | 1932 | 242.05       |             |            | 6.05        | 12.10      | 12.10      | 12.10      | 16.63        | 24.21      | 83.19       |
|  | 1934 | 49.86        |             |            |             | 1.25       | 2.49       |            | 3.43         | 4.99       | 12.16       |
|  | 1936 | 100.00       |             |            |             |            |            |            | 3.44         | 10.00      | 13.44       |
|  |      | \$25,049.04  | \$6,974.32  | \$1,156.43 | \$1,238.90  | \$1,244.95 | \$1,246.20 | \$1,247.44 | \$1,717.16   | \$1,663.37 | \$16,488.77 |
| (fol. 19)<br>Laundry Equipment:                                    | 1927 | \$4,103.21   | \$1,436.12  | \$205.16   | \$205.16    | \$205.16   | \$205.16   | \$205.16   | \$281.85     | \$205.17   | \$2,948.94  |
|  | 1928 | 175.00       | 44.75       | 8.75       | 8.75        | 8.75       | 8.75       | 8.75       | 12.02        | 17.50      | 118.02      |
|  | 1931 | 1,011.23     |             | 25.28      | 50.56       | 50.56      | 50.56      | 50.56      | 69.46        | 101.12     | 398.10      |
|  | 1932 | 2,447.35     |             |            | 61.18       | 122.37     | 122.37     | 122.37     | 168.10       | 244.74     | 841.13      |
|  |      | \$7,736.79   | \$1,480.87  | \$239.19   | \$325.65    | \$386.84   | \$386.84   | \$386.84   | \$531.43     | \$568.53   | \$4,306.19  |
| Ice Machine:   | 1927 | \$1,822.43   | \$637.84    | \$91.12    | \$91.12     | \$91.12    | \$91.12    | \$91.12    | \$125.18     | \$91.15    | \$1,309.77  |
|  | 1928 | 121.51       | 30.37       | 6.08       | 6.08        | 6.08       | 6.08       | 6.08       | 8.35         | 12.15      | 81.27       |
|  | 1929 | 325.00       | 48.75       | 16.25      | 16.25       | 16.25      | 16.25      | 16.25      | 22.32        | 32.50      | 184.82      |
|  | 1931 | 241.65       |             | 6.04       | 12.08       | 12.08      | 12.08      | 12.08      | 16.60        | 24.17      | 95.13       |
|  | 1932 | 53.68        |             |            | .84         | 1.68       | 1.68       | 1.68       | 2.32         | 3.37       | 11.57       |
|  | 1933 | 102.96       |             |            |             | 2.57       | 5.15       | 5.15       | 7.08         | 10.30      | 30.25       |
|  | 1936 | 75.00        |             |            |             |            |            |            | 2.58         | 7.50       | 10.08       |
|  |      | \$2,722.23   | \$716.96    | \$119.49   | \$126.37    | \$129.78   | \$132.36   | \$132.36   | \$184.43     | \$181.14   | \$1,722.89  |
| Ford Truck:  | 1933 | \$150.00     |             |            |             | \$18.75    | \$37.50    | \$37.50    | \$37.50      | \$18.75    | \$150.00    |
| Grand Totals   |      | \$133,250.53 | \$36,553.90 | \$6,410.71 | \$7,206.98  | \$7,364.73 | \$7,412.30 | \$7,475.71 | \$9,318.55   | \$7,864.02 | \$89,606.90 |
| Depreciation claimed on Income Returns                             |      |              | 36,553.90   | 12,532.05  | 14,102.55   | 14,409.36  | 11,909.41  | 11,179.84  | 12,456.02    | 7,864.02   | 121,007.15  |
| Excess Depreciation Deducted and not used to reduce Taxable Income |      |              | \$          | \$6,121.34 | \$6,895.57  | \$7,044.63 | \$4,497.11 | \$3,704.13 | \$3,137.47   | \$         | \$21,400.25 |
| Net Losses per Returns   |      |              | (Gain)      | \$8,912.97 | \$10,505.07 | \$8,879.33 | \$4,515.16 | \$6,511.52 | \$3,137.47   | (Gain)     |             |

NOTE:

- (1) Half rate 1937 additions..... \$24.90  
Add: To make total agree with amount claimed on return—\$932.87..... 24.01  
\$48.91
- (2) Depreciation allowable on 12½ year life..... \$2,398.08  
Depreciation claimed on return..... 924.56
- Additional depreciation allowable..... 1,473.52
- (3) Total depreciation claimed on return..... \$10,982.50  
Additional allowable on carpets (2)..... 1,473.52
- Total allowed but not less than allowable..... 12,456.02
- (4) Net loss—return..... \$1,663.95  
Additional allowable depreciation carpets (2)..... 1,473.52
- Corrected loss—return..... 3,137.47



[fol. 20]

## EXHIBIT "D" TO PETITION

Virginian Hotel Corporation of Lynchburg  
Lynchburg, Virginia

| Purchased               | Additions | Reserve<br>12-31-37 | Balance | Est. Life<br>Years | Years in<br>Service | Remaining<br>Life Years | Deprecia-<br>tion 1938 |
|-------------------------|-----------|---------------------|---------|--------------------|---------------------|-------------------------|------------------------|
| Furniture and Fixtures: |           |                     |         |                    |                     |                         |                        |

[fol. 20]

## EXHIBIT "D" TO PETITION

Virginian Hotel Corporation of Lynchburg  
Lynchburg, Virginia

## Furniture and Fixtures:

| Pur-<br>chased | Additions          | Reserve<br>12-31-37 | Balance            | Est. Life<br>Years | Years in<br>Service | Remaining<br>Life Years | Deprecia-<br>tion 1938 |
|----------------|--------------------|---------------------|--------------------|--------------------|---------------------|-------------------------|------------------------|
| 1927           | \$38,400.20        | \$27,597.82         | \$10,802.38        | 20                 | 10½                 | 9½                      | \$1,137.09             |
| 1927           | 1,730.33           | 1,243.59            | 486.74             | "                  | 10½                 | 9½                      | 51.24                  |
| 1928           | 3,087.23           | 2,064.38            | 1,022.85           | "                  | 9½                  | 10½                     | 97.41                  |
| 1929           | 692.35             | 393.76              | 298.59             | "                  | 8½                  | 11½                     | 25.96                  |
| 1930           | 1,789.54           | 838.74              | 950.80             | "                  | 7½                  | 12½                     | 76.06                  |
| 1931           | 15,033.55          | 5,918.57            | 9,114.98           | "                  | 6½                  | 13½                     | 675.18                 |
| 1932           | 2,733.92           | 939.63              | 1,794.29           | "                  | 5½                  | 14½                     | 123.74                 |
| 1934           | 999.63             | 243.61              | 756.02             | "                  | 3½                  | 16½                     | 45.82                  |
| 1935           | 184.57             | 40.21               | 144.36             | "                  | 2½                  | 17½                     | 8.25                   |
| 1936           | 134.76             | 18.11               | 116.65             | "                  | 1½                  | 18½                     | 6.31                   |
| 1937           | 544.85             | 27.24               | 517.61             | "                  | ½                   | 19½                     | 26.54                  |
| 1938           | 3,075.76           | .....               | 3,075.76           | "                  | ..                  | 20                      | 76.89                  |
|                | <u>\$68,406.69</u> | <u>\$39,325.66</u>  | <u>\$29,081.03</u> |                    |                     |                         | <u>\$2,350.49</u>      |

## Carpets:

|      |                    |                    |                   |     |    |     |                 |
|------|--------------------|--------------------|-------------------|-----|----|-----|-----------------|
| 1927 | \$19,341.70        | \$19,349.70        | \$.....           |     |    |     |                 |
| 1927 | 1,247.90           | 1,241.90           | .....             |     |    |     |                 |
| 1928 | 2,745.58           | 2,567.23           | 178.35            | 12½ | 9½ | 3   | \$59.45         |
| 1929 | 2,395.99           | 1,870.86           | 525.13            | "   | 8½ | 4   | 131.28          |
| 1931 | 4,406.74           | 2,291.51           | 2,115.23          | "   | 6½ | 6   | 352.54          |
| 1935 | 814.36             | 162.87             | 651.49            | "   | 2½ | 10  | 65.15           |
| 1936 | 386.73             | 82.41              | 604.32            | "   | 1½ | 11  | 54.94           |
| 1937 | 622.54             | 48.91              | 573.63            | "   | ½  | 12  | 47.80           |
| 1938 | 2,437.79           | .....              | 2,437.79          | "   | .. | 12½ | 97.51           |
|      | <u>\$34,699.33</u> | <u>\$27,613.39</u> | <u>\$7,085.94</u> |     |    |     | <u>\$808.67</u> |

## Improvements-Cafe:

|      |                    |                    |                   |    |     |     |                 |
|------|--------------------|--------------------|-------------------|----|-----|-----|-----------------|
| 1927 | \$7,232.40         | \$5,197.88         | \$2,034.52        | 20 | 10½ | 9½  | \$214.16        |
| 1927 | 9,599.67           | 6,899.17           | 2,700.50          | "  | 10½ | 9½  | 284.26          |
| 1928 | 3,894.13           | 2,603.97           | 1,290.16          | "  | 9½  | 10½ | 122.87          |
| 1929 | 659.08             | 374.78             | 284.30            | "  | 8½  | 11½ | 24.72           |
| 1930 | 214.81             | 100.67             | 114.14            | "  | 7½  | 12½ | 9.13            |
| 1931 | 3,057.04           | 1,203.51           | 1,853.53          | "  | 6½  | 13½ | 137.30          |
| 1932 | 242.05             | 83.19              | 158.86            | "  | 5½  | 14½ | 10.96           |
| 1934 | 49.86              | 12.16              | 37.70             | "  | 3½  | 16½ | 2.28            |
| 1936 | 100.00             | 13.44              | 86.56             | "  | 1½  | 18½ | 4.68            |
| 1938 | 915.97             | .....              | 915.97            | "  | ..  | 20  | 22.90           |
|      | <u>\$25,965.01</u> | <u>\$16,488.77</u> | <u>\$9,476.24</u> |    |     |     | <u>\$833.26</u> |

[fol. 21]

## Laundry Equipment:

|      |                   |                   |                   |    |     |     |                 |
|------|-------------------|-------------------|-------------------|----|-----|-----|-----------------|
| 1927 | \$4,103.21        | \$2,948.94        | \$1,154.27        | 20 | 10½ | 9½  | \$121.50        |
| 1928 | 175.00            | 118.02            | 56.98             | "  | 9½  | 10½ | 5.43            |
| 1931 | 1,011.23          | 398.10            | 613.13            | "  | 6½  | 13½ | 45.42           |
| 1932 | 2,447.35          | 841.13            | 1,606.22          | "  | 5½  | 14½ | 110.77          |
|      | <u>\$7,736.79</u> | <u>\$4,306.19</u> | <u>\$3,430.60</u> |    |     |     | <u>\$283.12</u> |

## Ice Machine:

|      |                   |                   |                   |    |     |     |                |
|------|-------------------|-------------------|-------------------|----|-----|-----|----------------|
| 1927 | \$1,822.43        | \$1,309.77        | \$512.66          | 20 | 10½ | 9½  | \$53.96        |
| 1928 | 121.51            | 81.27             | 40.24             | "  | 9½  | 10½ | 3.83           |
| 1929 | 325.00            | 184.82            | 140.18            | "  | 8½  | 11½ | 12.19          |
| 1931 | 241.65            | 95.13             | 146.52            | "  | 6½  | 13½ | 10.85          |
| 1932 | 33.68             | 11.57             | 22.11             | "  | 5½  | 14½ | 1.52           |
| 1933 | 102.96            | 30.25             | 72.71             | "  | 4½  | 15½ | 4.69           |
| 1936 | 75.00             | 10.08             | 64.92             | "  | 1½  | 18½ | 3.51           |
| 1938 | 268.44            | .....             | 268.44            | "  | ..  | 20  | 6.71           |
|      | <u>\$2,990.67</u> | <u>\$1,722.89</u> | <u>\$1,267.78</u> |    |     |     | <u>\$97.26</u> |

## Air Conditioning Equipment:

|      |                     |                    |                    |    |    |    |                   |
|------|---------------------|--------------------|--------------------|----|----|----|-------------------|
| 1938 | \$2,613.67          | \$.....            | \$2,613.67         | 20 | .. | 20 | \$65.34           |
|      | <u>\$142,412.16</u> | <u>\$89,456.90</u> | <u>\$52,955.26</u> |    |    |    | <u>\$4,438.14</u> |

[fol. 22]

[File endorsement omitted]

## BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

ANSWER—Filed January 30, 1941

Comes now the Commissioner of Internal Revenue by his Attorney J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein admits and denies as follows:

1. Admits that the petitioner is a corporation chartered and existing under and by virtue of the laws of the Commonwealth of Virginia, with its principal office at Church and Eighth Streets, Lynchburg, Virginia, and that its Federal income tax return for the calendar year 1938 was filed with the Collector of Internal Revenue for the District of Virginia at Richmond, Virginia.

2. Admits that a notice of deficiency was mailed to the petitioner on September 11, 1940, and that a true and correct copy of the said notice of deficiency is attached to the petition and marked Exhibit A. Denies that a true and correct copy of the Revenue Agent's Report is attached to the petition.

3. Admits that the taxes in controversy are Federal income and excess-profits taxes for the calendar year ended December 31, 1938, and that the deficiencies as determined by the Commissioner of Internal Revenue are \$416.94 and \$138.32, respectively.

[fol. 23] 4. Denies that the Commissioner of Internal Revenue erred in manner and form as set forth and alleged in sub-paragraphs (a), (b), (c), (d), and (e) of paragraph 4 of the petition.

5. Denies all of the allegations of fact as set forth and alleged in sub-paragraphs (a), (b), (c), (d), (e), (f), (g), (h), (i), and (j) of paragraph 5 of the petition.

6. Denies that the petitioner is entitled to the relief prayed for in sub-paragraphs (a), (b), and (c) of paragraph 6 of the petition.

7. Denies generally and specifically each and every allegation of fact contained in the petition not hereinbefore specifically admitted, qualified, or denied.

Wherefore, it is prayed that the appeal be denied.

(Signed) J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue.

Of Counsel: Chester A. Gwinn, Division Counsel; E. L. Corbin, Special Attorney, Bureau of Internal Revenue.  
elc/tls 1-27-41.

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[fol. 24]                      [File endorsement omitted]

BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

STIPULATION OF FACTS—Filed November 10, 1941

It is hereby stipulated and agreed by and between the parties hereto, by their respective agent and attorney, that the following facts are true and that the same may be so taken and considered by the Board of Tax Appeals as offered in evidence by the parties to this proceeding:

1. The petitioner is a corporation chartered under the laws of the State of Virginia in the year 1930. Its principal office is located at Church and Eighth Streets, Lynchburg, Virginia, and it has continuously since January 1, 1931, operated a hotel in the City of Lynchburg, Virginia, as lessee.

2. The petitioner filed its income tax return for the calendar year 1938 with the Collector of Internal Revenue for the District of Virginia, at Richmond, Virginia, and reported thereon a net taxable income of \$11,688.90.

3. The amount of \$4,341.97, depreciation, and the amount of \$70.00, Federal capital stock tax paid in the year 1938, were claimed as deductions from gross income on the said income tax return of the petitioner.

4. The respondent disallowed \$3,046.50 of the aforesaid depreciation deduction and all of the aforesaid \$70.00 Federal capital stock tax deduction and issued an alleged notice of deficiency, dated September 11, 1940, a copy of which is

attached to the petition of the petitioner heretofore filed in [fol. 25] this cause.

5. The Lynchburg Hotel Corporation caused a hotel, known as "The Virginian Hotel", to be erected at the corner of Church and Eighth Streets, Lynchburg, Virginia, about 1913, which has been leased to operating individuals and/or corporations at all times since its completion.

6. In 1927, prior to June 1st, the said hotel was operated by the Virginian Hotel, Incorporated, under a lease expiring on January 15, 1939, copy of which is attached and marked Exhibit A. The said hotel was completely furnished and equipped at this time, the furniture and equipment therein being the property of the lessee, the Virginian Hotel, Incorporated.

7. On June 1, 1927, with the written consent of the Lynchburg Hotel Corporation, the owner, A. F. Young and R. E. Young assumed the then existing lease of the said hotel and purchased from the Virginian Hotel, Incorporated, all of its furniture and equipment in the said hotel for the sum of \$70,899.94.

8. A. F. Young and R. E. Young operated the said hotel under the partnership name of "Virginian Hotel" from June 1, 1927, to December 31, 1930. Effective January 1, 1931, the said partnership was incorporated as the Virginian Hotel Corporation of Lynchburg, the petitioner herein, and all of the issued capital stock of the said corporation, 405 shares, par \$100.00, was issued to A. F. Young and R. E. Young, except qualifying shares, for the net book value of the partnership assets. "Values of the assets remained unchanged after the incorporation since no change in actual ownership was involved" (page 1, Preliminary [fol. 26] Statement, Exhibit B, annexed to petition). The said Virginian Hotel Corporation of Lynchburg, the petitioner herein, has continuously operated the said hotel since January 1, 1931, as lessee. No relationship has existed at any time between the holding corporation and the leasing corporation, their respective officers, directors and stockholders, other than lessor and lessee.

9. The total amount expended by the partnership and the petitioner for furniture and equipment, including replacements capitalized, from June 1, 1927, to December 31, 1938, is as follows:

| Purchased from prior Lessee June 1, 1927 ..... |            | Furniture<br>and Fixtures | Carpets     | Cafe<br>Improvements | Laundry<br>Equipment | Ice<br>Machine | Total        |
|--|------------|---------------------------|-------------|----------------------|----------------------|----------------|--------------|
|  |            | \$38,400.20               | \$19,341.70 | \$7,232.40           | \$4,103.21           | \$1,822.43     | \$70,899.94  |
| Additions                                      | 1927 ..... | \$1,730.33                | \$1,254.90  | \$9,599.67           | \$ .....             | \$ .....       | \$12,584.90  |
|  | 1928 ..... | 3,087.23                  | 2,745.58    | 3,894.13             | 175.00               | 121.51         | 10,023.45    |
|  | 1929 ..... | 692.35                    | 2,395.99    | 659.08               | .....                | 325.00         | 4,072.42     |
|  | 1930 ..... | 1,789.54                  | .....       | 214.81               | .....                | .....          | 1,997.35     |
|  | 1931 ..... | 15,033.55                 | 4,406.74    | 3,037.04             | 1,011.23             | 241.65         | 23,750.21    |
|  | 1932 ..... | 2,733.92                  | .....       | 242.05               | 2,447.35             | 33.68          | 5,457.00     |
|  | 1933 ..... | .....                     | .....       | .....                | .....                | 102.96         | 1,102.96     |
|  | 1934 ..... | 999.63                    | .....       | 49.86                | .....                | .....          | 1,049.49     |
|  | 1935 ..... | 184.57                    | 814.36      | .....                | .....                | .....          | 998.93       |
|  | 1936 ..... | 134.76                    | 686.73      | 100.00               | .....                | 75.00          | 996.49       |
|  | 1937 ..... | 544.85                    | 622.54      | .....                | .....                | .....          | 1,167.39     |
|  | 1938 ..... | 3,075.76                  | 2,437.79    | 915.97               | .....                | 268.44         | 6,697.96     |
| Total Additions .....                          |            | \$30,006.49               | \$15,357.63 | \$18,732.61          | \$3,633.58           | \$1,168.24     | \$68,898.55  |
| Grand Totals .....                             |            | \$68,406.69               | \$34,699.33 | \$25,965.01          | \$7,736.79           | \$2,990.67     | \$139,798.49 |



The above does not include the amount of \$2,613.67 expended in 1938 for air conditioning equipment, depreciation of which is not at issue herein.

[fol. 27] 10. Depreciation has been charged each year since June 1, 1927, at the following straight line rates, allowance having been made for fully depreciated items; and deductions have been claimed therefor on the income tax returns:

|                              |     |
|------------------------------|-----|
| Furniture and Fixtures ..... | 10% |
| Carpets .....                | 15% |
| Cafe Improvements .....      | 10% |
| Laundry Equipment .....      | 10% |
| Ice Machine .....            | 10% |

11. The respondent did not question the depreciation deduction as claimed each year through the year 1937. In arriving at the amount of depreciation allowable for the year 1938 the Revenue Agent determined that depreciation should be computed on the basis outlined on pages 5, 6, and 7 of Exhibit B annexed to the petition, which is by reference included in and made a part of this stipulation, and he computed the allowable depreciation for the year 1938 to be \$1,295.47 and disallowed \$3,046.50 of the amount claimed as a deduction by the petitioner.

12. The respondent approved the Revenue Agent's report and made it the basis of his notice of deficiency, from which the appeal was taken.

13. The partnership had a net gain for each of the years from June 1, 1927, to December 31, 1930, inclusive, and the entire amount of depreciation deducted on the income tax returns for those years served to reduce taxable income. The petitioner sustained a net loss for each of the years 1931, 1932, 1933, 1934, 1935 and 1936, and the entire amount of depreciation deducted on the income tax returns for those years did not serve to reduce the taxable income. The year 1937 resulted in a net gain and the depreciation deducted on the income tax return for that year served to reduce [fol. 28] taxable income. If the depreciation is recomputed for the years prior to the year 1938, using the amount claimed as a deduction for the years which resulted in a net gain and the amount allowable at the respondent's rates

as determined for 1938 for the years which resulted in a net loss, the results will be:

|   | Depreciation        |                    |                    | Net Loss           |
|---|---------------------|--------------------|--------------------|--------------------|
|   | Claimed             | Allowable          | Excess             | Tax Returns        |
| Years 1927-1930, inclusive                                      | \$36,553.90         | \$36,553.90        |                    | \$ Gain            |
| 1931  | 12,532.05           | 6,410.71           | \$6,121.34         | 8,912.97           |
| 1932  | 14,102.55           | 7,206.98           | 6,895.57           | 10,505.07          |
| 1933  | 14,409.36           | 7,364.73           | 7,044.63           | 8,872.33           |
| 1934  | 11,875.58           | 7,412.30           | 4,463.28           | 4,481.33           |
| Correction-Sch. L.,   |                     |                    |                    |                    |
| 1935  | 33.83               |                    |                    | + 33.83            |
| 1935  | 11,179.84           | 7,475.71           | 3,704.13           | 6,511.52           |
| 1936  | 10,982.50           | 9,318.55           | 3,137.47           | 1,663.95           |
| Correction resulting from<br>using respondent's rates<br>1931-5 | + 1,473.52          |                    |                    | +1,473.52          |
| 1937  | 7,864.02            | 7,864.02           |                    | Gain               |
| Totals  | <u>\$121,007.15</u> | <u>\$89,606.90</u> | <u>\$31,400.25</u> | <u>\$42,454.52</u> |

14. If the Board determines that the petitioner may recompute its depreciation for the years prior to the year 1938 as set forth above, and that the amount of \$31,400.25 may be restored to the undepreciated balance of the respective assets at December 31, 1937, the correct allowable depreciation for the year 1938, computed according to the respondent's rates, will be \$4,438.14. If the Board determines that the amount of \$31,400.25 may not be restored to the undepreciated balance then the correct allowable depreciation for 1938 will be \$1,295.47, and the Board may so enter its order.

15. The petitioner accrued at December 31, 1937, and deducted from gross income on its income tax return for the [fol. 29] calendar year 1937, a capital stock tax of \$55.00, computed according to the provisions of Section 105 of the Revenue Act of 1935 as amended by Section 401 of the Revenue Act of 1936, as follows:

|   |                    |
|---|--------------------|
| Adjusted Declared Value, June 30, 1937—Form |                    |
| 707   | \$48,336.05        |
| Additions:                                  |                    |
| Net Income for the year 1937                | 7,235.91           |
|   | <u>\$55,571.96</u> |
| Deductions                                  |                    |
|   | None               |
| Adjusted Declared Value, June 30, 1938      | <u>\$55,571.96</u> |
| Tax at \$1.00 for each \$1,000.00           | <u>\$55.00</u>     |

On filing its capital stock tax return for the capital stock tax year ended June 30, 1938, the petitioner declared a value of \$125,000.00 for its capital stock and showed a tax liability of \$125.00, or \$70.00 more than the amount that it had accrued at December 31, 1937.

16. The petitioner claimed the said \$70.00 additional capital stock tax paid in 1938 as a deduction from gross income on its income tax return for the calendar year 1938.

17. The respondent disallowed the said \$70.00 additional capital stock tax as a deduction from gross income for the calendar year 1938, and contends that it accrued July 1, 1937, and that it was an allowable deduction from gross income for the petitioner's calendar year 1937.

(Signed) O. H. Tufts, Agent for Petitioner. (Signed)  
J. P. Wenchel, R. E. S., Chief Counsel, Bureau of  
Internal Revenue.

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[fol. 30] EXHIBIT "A" TO STIPULATION OF FACTS

Virginian Hotel Corporation of Lynchburg—Docket No. 105828. Exhibit A annexed to Stipulation of Facts

This Contract and Lease made and entered into this 24th day of May, 1923, between The Lynchburg Hotel Corporation, a corporation organized and doing business under the laws of the State of Virginia, hereinafter styled "lessor", of the one part, and The Virginian Hotel, Incorporated, a corporation organized and doing business under the laws of the State of Virginia, hereinafter styled "lessee," of the other part,

Witnesseth: Whereas the contract of lease for the property of the said lessor in the City of Lynchburg, Va., known as "The Virginian Hotel," has been changed and amended several times by mutual consent; and

Whereas the parties hereto are the present lessor and lessee of the said property and have agreed to further changes and amendments of said contract of lease; and

Whereas it is deemed desirable to embody in this one formal contract and lease the entire agreement between the parties with respect to said property;

Now, therefore, in consideration of the premises and of the mutual obligations and liabilities herein assumed by

the parties hereto, the said parties do hereby contract and agree as follows:

I. That upon, and as of the date of, the execution hereof, all other contracts between the parties hereto with reference to the lease of the said property of the lessor, and especially the contract dated August 31st, 1911, between the lessor and R. L. O'Neal and C. C. Beeber, (which has been assumed by said lessee) and all amendments thereof, shall be, and are hereby, cancelled, annulled and abrogated, except as merged in this contract.

[fol. 31] II. The said lessor doth hereby lease, unto the said lessee, for the period hereinafter set forth that certain property of the lessor in the City of Lynchburg, Va., at the corner of Eighth and Church Streets, known as "The Virginian Hotel," with all the appurtenances thereto belonging or in any wise appertaining; and especially the right to use the alley in the rear of said Hotel for all purposes properly incident to the conduct of said Hotel, which said use of said alley shall not be unreasonably curtailed or restricted by grants of easements by the lessor to others for use thereof.

III. That said lessee shall continuously and uninterruptedly, throughout the term hereinafter specified, maintain and operate the said property as a first class, modern hotel; and shall likewise maintain the equipment, appointments and furnishings of said hotel in accordance with the standards of first class hotels of comparable size in Cities of like character and size to Lynchburg.

IV. That said lessor shall, as soon as practicable cause to be constructed upon the said hotel building an additional story containing additional rooms and shall at the same time cause the present assembly hall in said building to be converted and reconstructed into sleeping rooms. The said construction work shall be done in accordance with plans and specifications to be approved by said lessee. And it is specifically agreed that the natural and reasonable inconvenience to the operation of the said hotel by the lessee during the said construction work, shall not be the basis of any claim for abatement of rent during said period, nor of any claim for damages. Provided that this Clause shall not be construed as a waiver by the lessee of any right to assert proper claim for any physical damage that may be suffered

by it on account of the destruction of, or injury to, the said premises or any of its furniture, equipment or appointments, by said lessor or any of its agents in the course of said construction work.

[fol. 32] V. The said lessor shall keep an accurate account of its expenditures in the construction work to be done by it as herein set forth, and shall upon completion thereof; submit a statement of said account to the said lessee for inspection and audit. And upon the said completion of the said construction work, the said lessor shall turn over and deliver to the said lessee the said additional story and additional rooms for operation hereunder.

VI. The said lessee shall, at its own expense furnish and equip the said additional story and additional rooms as rapidly after said delivery thereof to it as the said additional rooms may be needed in the operation of the said hotel hereunder. And said furniture and equipment shall be of a character and quality in harmony and keeping with the present furniture and equipment of the said hotel as now operated.

VII. The said lessee shall insure, and keep continually insured, all of its furniture and equipment that is now in said hotel or that may hereafter be installed therein, for its fair value, in reputable insurance companies authorized and licensed to do business in the State of Virginia; and shall cause all policies of said insurance to be assigned to, or properly indorsed for, the protection of the said "lessor," and shall deliver said policies, as they shall be severally issued and renewed, to the said lessor.

VIII. The said lessee shall preserve all its furniture and equipment now in said hotel, or that may be hereafter installed therein, free from liens of every character that may lessen the value thereof as security to said lessor. And at any time that the said lessor may demand it, the said lessee shall cause a proper deed of trust to be executed, conveying all of said furniture and equipment to a trustee, in trust to secure the said lessor against any default of the said lessee in the performance of its obligations hereunder.

IX. The period of duration of this lease shall extend from the date of the execution hereof to the expiration of fifteen

[fol. 33] years after the completion of the additional story and additional rooms herein provided for, and the formal delivery thereof to said lessee for occupancy and operation hereunder.

X. The said lessee, as rent for the property hereby leased, from the execution hereof to the date of the completion and delivery of the additional story and additional rooms as hereinabove provided, shall pay to the said lessor an annual rental of twenty-four thousand dollars (\$24,000.00) payable in equal monthly installments on the first day of each calendar month. And from the said completion and delivery of the said additional story and additional rooms to the end of the full term of fifteen years thereafter, the said lessee shall pay an annual rental of twenty-four thousand dollars (\$24,000.00) plus an additional annual rental of a sum equal to 12% of the total amount expended by the said lessor in the actual construction of the said additional story and additional rooms, in accordance with the properly audited statement thereof as hereinabove provided. The said total annual rental from the date of said completion and delivery of the said additional story and additional rooms shall likewise be payable in equal monthly installments on the first day of each calendar month. It is specifically agreed between the parties hereto that in the event the taxes on the said leased property shall be increased during the term of this lease, either by increase of assessed value or of tax rate, over and above the amount of taxes applicable as of the date of the completion of the improvements herein provided for and their assessment for taxes as part of the leased premises, then the said lessee shall pay to the said lessor, as additional rental, a sum equal to the said *increase of taxes*, said amount to be due and payable with the October installments of rent in each year that such increased tax shall be payable by said lessor.

#### MARGINAL INDORSEMENT

It is understood and agreed between the Lunchburg Hotel Corporation and A. F. Young and Rosa E. Young, the assignees of this lease, that the monthly rent payable under this lease from June 1, 1927, until its expiration on January 15, 1939, is \$3165.77. This does not cover any addi-



tional charges for taxes as provided in Caluse X of this lease and the addition thereto.

Signed June 1, 1927. Lynchburg Hotel Corp. By J. T. Noell, Jr., Sec'y. A. F. Young, Rosa E. Young.

#### MARGINAL ENDORSEMENT

It is understood that "the said *increase* of taxes" to be paid the Lessor as provided in this paragraph, X, shall mean any increase in the sum total of all taxes—State, City and Federal that may be assessed against the Lynchburg Hotel Corporation.

J. T. Noell, Jr., Sec'y. F. C. Crider, Sec'y.

XI. In the event the said hotel shall be destroyed or rendered untenable as a hotel by fire or otherwise, without fault on the part of the lessee, then this lease shall terminate, and no rent shall accrue hereunder thereafter; [fol. 34] and no obligation shall rest upon either the lessor or lessee to rebuild the said hotel.

XII. In the event the said hotel be damaged by fire or otherwise, without fault on the part of the said lessee, not to the extent of rendering the same wholly untenable as a hotel, but only to the extent of depriving said lessee of the use of a part thereof, then such damage shall be repaired by said lessor as speedily as possible at its own expense; and there shall be such abatement of rent during the period of such deprival of the use of such damaged part of said hotel, as may be mutually agreed upon. And upon failure to so agree upon said abatement, each party shall select an arbitrator and these two arbitrators shall select a third, and the said arbitrators shall consider and determine the amount of said abatement. And the decision of said arbitrators shall be accepted by the parties thereto as final. Any expense involved in said arbitration shall be equally borne by the parties hereto.

XIII. Except as specifically provided in Clause XI and XII hereinabove, the said lessee shall keep the leased premises continuously in good repair at its own expense; and at the expiration of this lease said lessee shall restore said premises to the lessor in as good condition as at the commencement hereof reasonable wear and tear excepted.



XIV. The said lessee shall not sub-lease the said property hereby leased to any other person, firm or corporation, without the written consent of the said lessor. But this Clause shall not be construed to restrict the right of said lessee, which is hereby specifically granted, to sub-lease portions of the said building for purposes not inconsistent with its operation as a hotel as herein provided.

XV. The lessee shall have the right, and hereby assumes the obligation, to alter and reconstruct at its expense the main floor of said hotel so as to provide for additional cafes or dining rooms at the front of said building, and so as to convert the present main dining room into an Assembly Hall. Provided that said alterations shall be in accordance with plans and specifications to be approved by the lessor. And it is understood that this improvement when completed shall belong absolutely to the lessor without any obligation on its part to refund the cost of same to the lessee.

[fol. 35] XVI. As further consideration for the execution hereof R. L. O'Neal, the principal stockholder in said lessee, agrees that he will not during the term of this lease, voluntarily sell, convey or transfer the controlling stock ownership in said lessee to any other person, without the consent of the lessor. And the said R. L. O'Neal executes this contract in his individual capacity as an evidence of said agreement.

In Testimony Whereof, The Lynchburg Hotel Corporation and The Virginian Hotel, Incorporated have caused this agreement and lease to be signed in duplicate by their respective Presidents; and have caused their corporate seals to be hereunto affixed and attested by their respective Secretaries, the day and date first above written.

The Lynchburg Hotel Corporation, by O. B. Barker, Vice-President. Attest: J. T. Noell, Jr., Secretary. (Seal) The Virginian Hotel, Incorporated, By R. L. O'Neal, President. Attest: F. C. Crider, Secretary. (Seal) R. L. O'Neal.

[Notary acknowledgments omitted in copy.]

[fol. 36]

## CONSENT TO ASSIGNMENT

The Lynchburg Hotel Corporation does hereby consent to the assignment by The Virginian Hotel, Incorporated, to Albert F. Young and Rosa E. Young, of the lease on the Virginian Hotel property in the city of Lynchburg at the corner of Church and Eighth Streets, dated May 24th, 1923, and to which lease this consent is attached, and does hereby release and discharge The Virginian Hotel, Incorporated, from any liability or obligations as lessee under said lease, from and after the date hereof, and does look to the said Albert F. Young and Rosa E. Young for the performance of all obligations and payments under the said lease. The said Albert F. Young and Rosa E. Young do, by their signatures hereto, expressly assume all obligations and payments under said lease from this date.

In testimony whereof the Lynchburg Hotel Corporation has caused this consent to be hereon endorsed and signed on its behalf this first day of June, 1927, by John W. Craddock, its President, thereunto specifically authorized by its Board of Directors by resolution duly adopted by its Board of Directors at a meeting of said Board held on May 16th, 1927; and the said Albert F. Young and Rosa E. Young, have likewise signed this consent on this 1st day of June, 1927.

Lynchburg Hotel Corporation, By John W. Craddock, President. Attest: J. T. Noell, Jr. Sec'y.  
(Seal) Rosa E. Young, A. F. Young.

[fol. 37] BEFORE UNITED STATES BOARD OF TAX APPEALS  
VIRGINIAN HOTEL CORPORATION OF LYNCHBURG, Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No. 105828

*O. H. Tufts, C. P. A.* for petitioner.

*E. L. Corbin, Esq.,* for the respondent.

MEMORANDUM OPINION

ARNOLD:

The Commissioner determined deficiencies in income and excess profits taxes for the year 1938 in the amounts of \$416.94 and \$138.32, respectively. The questions involved are (1) whether petitioner is entitled to restore to its unexhausted base of depreciable assets on December 31, 1937, the amount of \$31,400.25 due to a change in rates of depreciation by respondent; and (2) whether petitioner is entitled to a deduction of \$70 representing additional capital stock tax paid in 1938. The respondent on brief concedes that petitioner is entitled to the claimed deduction of \$70. This deduction will, therefore, be allowed upon recomputation under Rule 50. The facts were stipulated and are included herein by reference.

The petitioner is a Virginia corporation and was incorporated in 1930. It has since January 1, 1931, operated a hotel in Lynchburg, Virginia, as lessee. It filed its income tax return for 1938 with the collector of internal revenue for the District of Virginia at Richmond, Virginia, and reported thereon a net taxable income of \$11,688.90.

About 1913 Lynchburg Hotel Corporation cause a hotel known as "The Virginian Hotel" to be erected in Lynchburg, Virginia, which hotel at all times since its completion has been leased to operating individuals and/or corporations. Prior to June 1, 1927, the hotel was operated by Virginia Hotel, Incorporated, under a lease dated May 24, 1923, and expiring January 15, 1939. The hotel was completely furnished and equipped, the furniture and equipment therein being the property of the lessee. On June 1, 1927, with the consent of the owner lessor, A. F. Young and

R. E. Young, assumed the then existing lease of the hotel and purchased from the lessee all of its furniture and equipment for the sum of \$70,899.94. A. F. and R. E. Young operated the hotel under the partnership name of "Virginian Hotel" from June 1, 1927 to December 31, 1930. The partnership was incorporated as the Virginian Hotel Corporation of Lynchburg, the petitioner herein, and all of its issued capital stock, except qualifying shares, was issued to A. F. and R. E. Young for the net book value of the partnership assets. The petitioner has continuously operated the hotel since January 1, 1931, as lessee.

The total amount expended by the partnership and the petitioner for furniture and equipment, including replacements capitalized from June 1, 1927 to December 31, 1938, is as follows:

[fol. 38]

|   | Furniture<br>and Fixtures | Carpets     | Cafe<br>Improvements | Laundry<br>Equipment | Ice<br>Machine | Total        |
|---|---------------------------|-------------|----------------------|----------------------|----------------|--------------|
| Purchased from prior Lessee June 1, 1927..... | \$38,400.20               | \$19,341.70 | \$7,232.40           | \$4,103.21           | \$1,822.43     | \$70,899.94  |
| Additions 1927.....                           | \$1,730.33                | \$1,254.90  | \$9,599.67           | \$.....              | \$.....        | \$12,584.90  |
| 1928.....                                     | 3,087.23                  | 2,745.58    | 3,894.13             | 175.00               | 121.51         | 10,023.45    |
| 1929.....                                     | 692.35                    | 2,395.99    | 659.08               | .....                | 325.00         | 4,072.42     |
| 1930.....                                     | 1,789.54                  | .....       | 214.81               | .....                | .....          | 1,997.35     |
| 1931.....                                     | 15,033.55                 | 4,406.74    | 3,057.04             | 1,011.23             | 241.65         | 23,750.21    |
| 1932.....                                     | 2,733.92                  | .....       | 242.05               | 2,447.35             | 33.68          | 5,457.00     |
| 1933.....                                     | .....                     | .....       | .....                | .....                | 102.96         | 102.96       |
| 1934.....                                     | 999.63                    | .....       | 49.86                | .....                | .....          | 1,049.49     |
| 1935.....                                     | 184.57                    | 814.36      | .....                | .....                | .....          | 998.93       |
| 1936.....                                     | 134.76                    | 686.73      | 100.00               | .....                | 75.00          | 996.49       |
| 1937.....                                     | 544.85                    | 622.54      | .....                | .....                | .....          | 1,167.39     |
| 1938.....                                     | 3,075.76                  | 2,437.79    | 915.97               | .....                | 268.44         | 6,667.96     |
| Total Additions.....                          | \$30,006.49               | \$15,357.63 | \$18,732.61          | \$3,633.58           | \$1,168.24     | \$68,898.55  |
| Grand Totals.....                             | \$68,406.69               | \$34,699.33 | \$25,965.01          | \$7,736.79           | \$2,990.67     | \$139,798.49 |

The above does not include the amount of \$2,613.67 expended in 1938 for air conditioning equipment, depreciation of which is not at issue herein.

Depreciation was charged and deductions claimed on income tax returns each year since June 1, 1927, at the following straight line rates, allowance having been made for fully depreciated items:

|                        |     |
|------------------------|-----|
| Furniture and Fixtures | 10% |
| Carpets                | 15% |
| Cafe improvements      | 10% |
| Laundry Equipment      | 10% |
| Ice Machine            | 10% |

The respondent did not question the depreciation deduction as claimed each year through the year 1937. In 1938 the petitioner claimed a depreciation deduction based on the above rates amounting to \$4,341.97. After an examination of petitioner's income tax return for 1938 the respondent determined that the depreciation claimed was excessive, that the average useful life of the depreciable assets from the time of acquisition in 1927 was as follows, and applied rates accordingly:

| Assets                 | Average<br>Useful Life | Rate |
|------------------------|------------------------|------|
| Furniture and Fixtures | 20 Years               | 5%   |
| Carpets                | 12½ years              | 8%   |
| Cafe Improvements      | 20 years               | 5%   |
| Laundry Equipment      | 20 "                   | 5%   |
| Ice Machine            | 20 "                   | 5%   |

As a result he disallowed \$3,046.50 of the amount of depreciation claimed by the petitioner in its return, thus allowing a deduction in the amount of \$1,295.47.

[fol. 39] The partnership had a net gain for each of the years from June 1, 1927 to December 31, 1930, inclusive, and the entire amount of depreciation deducted in its returns for those years served to reduce taxable income. The petitioner sustained a net loss for each of the years 1931 to 1936, both inclusive, and the entire amount of depreciation deducted in its returns for those years did not serve to reduce its taxable income. The year 1937 resulted in a net gain and the depreciation deducted on the income tax return for that year served to reduce taxable income. Re-

computing the depreciation for the years prior to 1938, using the amount claimed as a deduction for the years which resulted in a net gain and the amount allowable at the respondent's rates as determined for 1938 for the years which resulted in a net loss, the excess depreciation claimed over the amount allowable is \$31,400.25. This amount did not serve to reduce taxable income. Restoring the amount of \$31,400.25 to petitioner's unexhausted depreciation base as of December 31, 1937, the correct allowable depreciation for the year 1938, applying respondent's rates, is \$4,438.14.

The petition does not question the respondent's determination of the average useful life of the depreciable assets involved nor the rates to be used. It contends that since the petitioner sustained net losses in each of the years 1931 to 1936, both inclusive, and since depreciation claimed in the amount of \$31,400.25 in excess of the amount allowable as determined by respondent did not serve to reduce taxable income in such years, that such amount should be restored to its depreciation base as of December 31, 1937.

The Board held in *Kennedy Laundry Company*, 46 B. T. A. 70, following the ruling in *Pittsburgh Brewing Co. v. Commissioner*, 107 Fed. (2d) 155, that depreciation is not "allowed" within the meaning of the revenue acts unless it is actually taken as a deduction against taxable income, that to the extent the taxpayer received no tax advantage in certain years prior to the taxable year in which it had sustained net losses, its base for depreciation should be computed by employing the lower rate determined by respondent for such years instead of the rate used by it. This decision is controlling herein. See *Don Lee, Inc., v. United States*, 42 Fed. Supp. 884. The amount of \$31,400.25, the excess of depreciation deductions taken in the years 1931 to 1936, inclusive, over the amounts allowable, should be added to the base in computing the depreciation allowable for 1938. The amount so allowable was stipulated to be \$4,438.14.

*Decision will be entered under Rule 50.*

Entered: May 6, 1942.



[fol. 40] BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 105828

VIRGINIAN HOTEL CORPORATION OF LYNCHBURG, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

### DECISION

Pursuant to the memorandum opinion of the Board entered May 6, 1942, the petitioner on May 13, 1942 filed a recomputation of tax and on May 25, 1942 the respondent filed a recomputation in agreement with that of petitioner. Now, therefore, it is

Ordered and Decided: That there is an overpayment of income tax for the calendar year 1938 in the amount of \$13.47, which amount was paid within three years before the filing of the petition (Sec. 322(d), Revenue Act of 1938); and that there is no deficiency in excess-profits tax for said year 1938.

Enter:

(s) William W. Arnold, Member.

Entered May 28, 1942.

[fol. 41] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR  
THE FOURTH CIRCUIT

[Title omitted]

PETITION FOR REVIEW—Filed August 18, 1942

Guy T. Helvering, Commissioner of Internal Revenue, holding office by virtue of the laws of the United States, hereby petitions the United States Circuit Court of Appeals for the Fourth Circuit to review the decision entered May 28, 1942, ordering and deciding that there is an overpayment of income tax for the taxable year 1938 in the amount of \$13.47 due Virginian Hotel Corporation of Lynchburg, the respondent on review herein, and that there is no deficiency in excess-profits tax for said year 1938 due by the respondent on review herein. This petition for review is filed pursuant to the provisions of Sections 1141 and 1142 of the United States Internal Revenue Code.

The respondent on review, Virginian Hotel Corporation of Lynchburg, filed its income tax return for the taxable year 1938 with the Collector of Internal Revenue for the District of Virginia, located at Richmond, Virginia, the office of which Collector is within the jurisdiction of the United States Circuit Court of Appeals for the Fourth Circuit, wherein this review is sought.

(Signed) Samuel O. Clark, Jr., Assistant Attorney General; (Signed) J. P. Wenchel, RLW, Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.

Of Counsel: Claude R. Marshall, Special Attorney, Bureau of Internal Revenue.

CRM/csl. 8/1942.

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[fol. 42] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR  
THE FOURTH CIRCUIT

[Title omitted]

NOTICE OF FILING PETITION FOR REVIEW—Filed August 25,  
1942

To: O. H. Tufts, C. P. A., Krise Building, Lynchburg, Virginia.

You are hereby notified that the Commissioner of Internal Revenue did, on the 18th day of August, 1942, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Fourth Circuit, of the decision of the Board heretofore rendered in the above-entitled cause. A copy of the petition for review as filed is hereto attached and served upon you.

Dated this 18th day of August, 1942.

(S.) B. D. Gamble, Clerk, U. S. Board of Tax Appeals.

Service of the above and foregoing notice, together with a copy of the petition for review, is hereby acknowledged this 24 day of August, 1942.

Agent: (S.) O. H. Tufts, Attorney for Respondent on Review.

CRM/csl. 8/42.

[fol. 43] [File endorsement omitted]

IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR  
FOURTH CIRCUIT

[Title omitted]

NOTICE OF FILING PETITION FOR REVIEW—Filed August 26,  
1942

To: A. F. Young, President of Virginian Hotel Corporation  
of Lynchburg, Church and Eighth Streets, Lynchburg,  
Virginia.

You are hereby notified that the Commissioner of Internal Revenue did, on the 18th day of August, 1942, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Fourth Circuit, of the decision of the Board heretofore rendered in the above-entitled cause. A copy of the petition for review as filed is hereto attached and served upon you.

Dated this 18th day of August, 1942.

(Signed) J. P. Wenchel, RLW, Chief Counsel, Bureau  
of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review, is hereby acknowledged this 20 day of Aug., 1942. (Sgd.) A. J. Young, Pres., For Respondent on Review.

8/42. CRM/csl.

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[fol. 44] [File endorsement omitted]

IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE  
FOURTH CIRCUIT

[Title omitted]

STATEMENT OF POINTS—Filed September 9, 1942

Now Comes Guy T. Helvering, Commissioner of Internal Revenue, the petitioner on review herein, by and through his attorneys, Samuel O. Clark, Jr., Assistant Attorney General, and J. P. Wenchel, Chief Counsel, Bureau of In-

ternal Revenue, and hereby asserts the following errors which he intends to rely on this review:

*That the United States Board of Tax Appeals erred:*

1. In holding and deciding that taxpayer's base for furniture, fixtures and equipment as of December 31, 1937 should be computed by deducting depreciation for the years 1931 to 1936, both inclusive, at the lower rates determined as reasonable by the Commissioner for the year 1938 instead of at the higher rates used by taxpayer for the years 1931 to 1936, inclusive.

2. In holding and deciding that, to the extent that taxpayer received no tax advantage in the years 1931 to 1936, both inclusive, taxpayer's base for depreciation as of December 31, 1937 should be computed by employing the lower rates for the said years 1931 to 1936, both inclusive, that were determined by the Commissioner as reasonable for the year 1938.

3. In holding and deciding that depreciation is not "allowed" within the meaning of Section 113 (b) (1) (B) of the Revenue Act of 1938, unless it is actually taken as a deduction against taxable income and taxable advantage is obtained thereby.

[fol. 45] 4. In holding and deciding that the aggregate amount of \$31,400.25, representing alleged excessive depreciation deductions taken in the years 1931 to 1936, inclusive, should be restored to the cost of taxpayer's depreciable assets as of December 31, 1937 for the purpose of computing depreciation for 1938.

5. In holding and finding that the alleged excessive depreciation in the amount of \$31,400.25 for the years 1931 to 1936, inclusive, did not serve to reduce taxable income in said years, there being no substantial evidence to support such a holding and finding.

6. In holding and finding that taxpayer is entitled to a deduction for depreciation in the year 1938 in the amount of \$4,438.14.

7. In failing to hold and find that taxpayer is entitled to a deduction for depreciation in the year 1938 only in the amount of \$1,295.47.

8. In that its opinion and decision are not supported by its findings of fact and are contrary to the law and the regulations.

9. In ordering and deciding that there is an overpayment in income tax of \$13.47 for the year 1938.

10. In ordering and deciding that there is no deficiency in excess-profits tax for the year 1938.

11. In failing to order and decide that there is a deficiency in income tax for the year 1938 due from taxpayer herein in the amount of \$416.94.

12. In failing to order and decide that there is a deficiency in excess-profits tax for the year 1938 due from the taxpayer herein in the amount of \$138.32.

(Signed) Samuel O. Clark, Jr., Assistant Attorney General; (Signed) J. P. Wenchel, RLW, Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.

CRM/csl. 8/42.

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[fol. 46] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR  
THE FOURTH CIRCUIT

[File endorsement omitted]

DESIGNATION OF PORTIONS OF RECORD, PROCEEDINGS AND EVIDENCE TO BE CONTAINED IN RECORD ON REVIEW—

Filed Sept. 9, 1942

*To the Clerk of the United States Board of Tax Appeals:*

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Fourth Circuit, copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Fourth Circuit, heretofore filed by the Commissioner of Internal Revenue:

1. Docket entries of the proceedings before the Board.
2. Pleadings before the Board:

(a) Petition, including annexed copy of deficiency letter and all exhibits attached.

(b) Answer.

3. Stipulation of Facts.

4. Memorandum opinion of the Board entered on May 6, 1942.

5. Board's decision entered on May 28, 1942.

6. Petition for review, together with proof of service of notice of filing petition for review and of service of a copy of petition for review.

7. Statement of Points to be relied upon.

[fol. 47] 8. Any and all orders of enlargement of time for the preparation of the evidence and for the transmission and delivery of the record.

9. This Designation.

Said transcript to be prepared, certified and transmitted as required by law and the rules of the United States Circuit Court of Appeals for the Fourth Circuit.

(Signed) J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, Attorney for Petitioner on Review.

[fol. 48] Clerk's Certificate to foregoing transcript omitted in printing.

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[fol. 49] IN THE UNITED STATES CIRCUIT COURT OF APPEALS  
FOR THE FOURTH CIRCUIT

No. 5004

GUY T. HELVERING, Commissioner of Internal Revenue,  
Petitioner,

*versus*

VIRGINIAN HOTEL CORPORATION OF LYNCHBURG, Respondent  
ON PETITION TO REVIEW THE DECISION OF THE UNITED STATES  
BOARD OF TAX APPEALS

#### DOCKET ENTRIES

September 25, 1942. the transcript of record is filed and the cause docketed.

September 29, 1942, the appearance of Frank G. Davidson, Jr., is entered for the respondent.

Same day, the appearance of Samuel O. Clark, Jr., Assistant Attorney General, and Sewall Key, Special Assistant to the Attorney General, is entered for the petitioner.

September 30, 1942, the appearance of J. P. Wenchel, Chief, Counsel, Bureau of Internal Revenue, and Claude R. Marshall, Special Attorney, Bureau of Internal Revenue, is entered for the petitioner.

October 14, 1942, the appearance of L. W. Post, Special Assistant to the Attorney General, is entered for the petitioner.

[fol. 50] Same day, to-wit, October 14, 1942, brief and appendix on behalf of the petitioner are filed.

October 31, 1942, brief on behalf of the respondent is filed.

#### ARGUMENT OF CAUSE

November 17, 1942 (November term, 1942), cause came on to be heard before Parker and Soper, Circuit Judges, and Chesnut, District Judge, and was argued by counsel and submitted.

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[fol. 51] IN UNITED STATES CIRCUIT COURT OF APPEALS,  
FOURTH CIRCUIT

No. 5004

GUY T. HELVERING, Commissioner of Internal Revenue,  
Petitioner,

*versus*

VIRGINIAN HOTEL CORPORATION OF LYNCHBURG, Respondent

On Petition to Review the Decision of the United States  
Board of Tax Appeals

(Argued November 17, 1942. Decided January 2, 1943)

Before Parker and Soper, Circuit Judges, and Chesnut,  
District Judge

L. W. Post, Special Assistant to the Attorney General,  
(Samuel O. Clark, Jr., Assistant Attorney General, and  
Sewall Key, Special Assistant to the Attorney General,  
on brief) for Petitioner, and Frank G. Davidson, Jr., for  
Respondent.



## OPINION—Filed January 2, 1943

[fol. 52] Parker, Circuit Judge:

This is a petition to review a decision of the Board of Tax Appeals (now the Tax Court of the United States). The question involved relates to the right of a taxpayer to add to the depreciation base, on a change of the rate of depreciation, amounts charged off and allowed as depreciation in prior years, where no tax benefit has been received as a result of such allowance. The contention of the taxpayer is that the new rate of depreciation should be applied retroactively, and that the excess depreciation charged off and deducted under the old rate should be restored to the base, when it appears that the taxpayer has received no tax benefit from the deduction. The Board sustained this contention and the Commissioner has asked that its decision be reviewed, contending that there is no authority for restoring to the base the depreciation which has been claimed and allowed, and that whether tax benefit has resulted from the allowance or not does not affect the matter.

Taxpayer is a corporation which has operated a hotel in Lynchburg, Va., since January 1, 1931. In making its tax returns from that time through the year 1937, it claimed and was allowed depreciation at straight line rates of 10% on all of its equipment except carpets and upon these at 15%, based upon an estimated useful life of 10 and 6½ years respectively. For the year 1938 the taxpayer claimed a deduction for depreciation at the same rates; but the Commissioner determined that the useful life of the equipment had been underestimated and that the rates of depreciation allowed were excessive. The useful life of the equipment except carpets was estimated at 20 years and carpets at 12½ years. From the cost of the property, the depreciation theretofore allowed was deducted, and the remainder was taken as the new base for computing depreciation. The rate was arrived at on the basis of what remained of useful life. Thus on an item of \$15,033.55, which had been in service 6½ years, and upon which depreciation [fol. 53] of \$9,771.83 had been taken and allowed, the Commissioner found there was a value of \$5,261.72 remaining, with a useful life of 13½ years, and allowed annual depreciation of \$389.76, or an amount which taken annually for 13½ years would liquidate the remaining value.

The contention of taxpayer is that, instead of doing this, the Commissioner, when putting the new rates of depreciation into effect, should have restored to the base so much of the depreciation shown on its returns for the years 1931 to 1937 as did not reduce its taxable income in those years and was in excess of the amounts of the deductions to which it would have been entitled at the rates of depreciation now determined by the Commissioner to be reasonable. This amount was \$31,400.25 and represented the excess of depreciation for the years 1931 to 1936 inclusive, for which the returns of taxpayer showed a net loss. No contention is made with respect to the depreciation for the year 1937, in which the return showed a net gain. It is stipulated that for the years 1931 to 1936 the deduction of depreciation did not serve to reduce the taxable income.

The statute involved is the *Revenue Act* of 1938, 52 Stat. 447. Sec. 23(1) of that statute, under the heading "Depreciation," allows as a deduction from gross income "a reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence." Sec. 23(n) provides that the basis upon which such depreciation shall be allowed is that provided in sec. 114, which is the section that gives the basis for determining the gain upon the sale or other disposition of property. Sec. 114 provides that the basis for determining depreciation shall be the "adjusted basis" of sec. 113(b); and sec. 113(b) provides that proper adjustment shall be made "for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the amount allowable) under this act or prior income tax laws." It is clear, therefore, that the basis for computing depreciation is that which must be [fol. 54] taken for computing gain upon the sale of the property, and that depreciation theretofore allowed or allowable under the income tax laws must be deducted from the base. The applicable statutes are as follows:

"Sec. 23. Deductions from gross income.

"In computing net income there shall be allowed as deductions:

• • • • •

“(1) Depreciation.—A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence.

“(n) Basis for depreciation and depletion.—The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be as provided in section 114.

“Sec. 113. Adjusted Basis for determining gain or loss.

“(b) Adjusted basis.—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

“(1) General rule.—Proper adjustment in respect of the property shall in all cases be made—

“(B) in respect of any period since February 28, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the amount allowable) under this Act or prior income tax laws.

[fol. 55] “Sec. 114. Basis for depreciation and depletion.

“(a) Basis for depreciation.—The basis upon which exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be the adjusted basis provided in section 113(b) for the purpose of determining the gain upon the sale or other disposition of such property.”

We think that the Board was in error in holding that depreciation claimed and allowed should be deducted from the base in determining gain under sec. 114 only where it has resulted in tax benefit. Depreciation amounts to the sale of property through use; and the intention of Congress is clear that to the extent that depreciation has been allowable under

the law or to the extent that it has been allowed in determining tax liability, it is to be excluded from the value of the property in determining profits from sale or base for allowance of depreciation. There is nothing in the statute, or elsewhere, which justifies restoring to the base the depreciation which has been claimed and allowed in prior returns, merely because such allowance has resulted in no tax benefit (Cf. *Mother Lode Coalition Mines Co. v. Helvering*, — U. S. — (decided Dec. 7, 1942); and such restoration is directly in conflict with the statutory provision that adjustment shall be made for depreciation to the extent allowed under the act or prior income tax laws. It is in conflict, too, with the salutary rule that each taxable year must be regarded as an independent unit for income tax purposes. *Burnet v. Sanford & Brooks Co.*, 282 U. S. 359.

It is argued that the word "allowed" as used in the statute means taken as a deduction from income tax paid; but, as pointed out in the dissenting opinion of Member Disney in the case of *Kennedy Laundry Co. v. Commissioner*, 46 B. T. A. —, decided January 14, 1942, "In ordinary parlance or thought as to income tax matters the word 'allowed' means in effect 'considered in arriving at the net tax result for the year', and in my opinion that is all that Congress intended in the section here being considered." This is in [fol. 56] accord with our decision in *Helvering v. State-Planters Bank & Trust Co.*, 4 Cir. 130 F. 2d 44. The regulation there dealt with provided that the collection of a bad debt should be included in income if the bad debt had previously been "charged off and allowed as a deduction for income tax purposes". We rejected the argument that tax benefit as a result of the deduction was necessary for the inclusion of collections on the debt as income, saying:

"There is nothing in the regulation or in any statute which makes the inclusion in gross income of collections on bad debts, previously charged off as worthless, dependent upon whether or not the charge off has resulted in a tax benefit to the taxpayer. It is argued that the language of the regulation providing for the inclusion of the collection only where the debt has been 'charged off and allowed as a deduction for income tax purposes' has this effect; but manifestly a debt is charged off and allowed as a deduction for income tax purposes when it is claimed and allowed as a deduction in the return of the taxpayer, for the charge off and allowance is made in connection with the return, not

in connection with the payment of the tax.” (Italics supplied.)

Prior to the Revenue Act of 1932, provision was made in the Revenue Act of 1926 and subsequent acts for diminution of the base by the amount allowable for depreciation. In the Act of 1932, the provision contained in the 1938 Act was inserted for the first time requiring adjustment for depreciation “to the extent allowed (but not less than the amount allowable)”. The purpose of the amendment, as explained in the report of the Senate Committee, was to preclude the possibility of a taxpayer’s claiming, on the sale of property, that the depreciation allowed in connection with prior returns was excessive. *S. Rep. No. 665, 72nd Cong., 1st Sess. p. 29.* The Supreme Court had held that the amount allowable for depreciation must be deducted whether taken in prior returns or not (*United States v. Ludey*, 274 U. S. 295); and the effect of the amendment was to place depreciation, to the extent that it had been allowed, on the same basis [fol. 57] as allowable depreciation under prior acts. The history and purpose of the amendment are correctly set forth, we think, in the dissenting opinion of Member Disney in the *Kennedy Laundry Company* case, as follows:

“The word ‘allowed’ was first used in this respect in sec. 202(b), Revenue Act of 1924, where adjustment is required in computing gain or loss from sale or other disposition of property for wear and tear ‘previously allowed with respect to such property.’ It appears from the committee reports in connection with that statute that in the form the bill had taken in the House the words ‘properly chargeable’ were used, and on this subject the Senate Committee Report says: ‘To remove a possible ambiguity in the House Bill, the deductions are limited to those “previously allowed” rather than those “properly chargeable”.’ The Revenue Act of 1926, section 202(b), changed the expression to ‘allowable’, which was by section 113(b)(1)(B) of the Revenue Act of 1932 changed to ‘extent allowed (but not less than the amount allowable)’. It seems to me that Congress in 1932, as it did in 1924, used the word ‘allowed’ in order ‘to remove a possible ambiguity’, that is, intended in order to make the matter definite, to say that if a depreciation item was ‘allowed’ in the sense that a claim therefor was not opposed or the depreciation was given effect in determining the tax situation for the year involved, it was to constitute a ground



for adjustment of base for the property considered. I think that was all that Congress had in mind and that the legislators did not go into more tenuous consideration of tax advantage, or lack thereof in the year of depreciation, but laid down a definite and not unfair rule. The taxpayer had the opportunity of preventing the 'allowance' of more depreciation than necessary (above the 'amount allowable' or reasonable amount). He could limit his claim, withdraw it to any extent desired, or oppose its use by the Commissioner. This being within his power, there is no injustice in requiring him, when property basis is considered in later years, to abide by the figure used by him, or permitted by him to be used."

There was no intention to authorize retroactive adjustments. With respect to this, the report of the Senate Committee referred to above had the following to say:

[fol. 58] "Your committee has not thought it necessary to include any express provision against retroactive adjustments of depreciation on the part of the Treasury as the regulations of the Treasury seem adequate to protect the interests of taxpayers in such cases. These regulations require the depreciation allowances to be made from year to year in accordance with the then known facts and do not permit a retroactive change in these allowances by reason of the facts developed or ascertained after the years for which such allowances are made."

It is well settled that allowable depreciation must be deducted from cost in arriving at the base under secs. 114 and 113(b) even though the deduction of depreciation in prior returns has resulted in no tax benefit, and even though depreciation may not have been deducted at all in prior returns. *United States v. Ludey, supra*; *Hardwick Realty Co. v. Commissioner*, 2 Cir. 29 F. 2d 498; *Beckridge Corp. v. Commissioner*, 2 Cir. 129 F. 2d 318. This is unquestionably a holding that the question of tax benefit is immaterial. As stated above, the effect of the 1932 change in the Revenue Act is to put depreciation allowed in the same category.

In the decision in the *State-Planters Bank & Trust Co. case*, we pointed out the analogy between the situations presented in the case of the collection of a debt previously charged off as worthless and the sale of property at a price in excess of cost less depreciation, and relied upon the Su-

preme Court's decision in *United States v. Ludey*, *supra*, as sustaining our decision that an inquiry as to whether the deduction had resulted in tax benefit was irrelevant. We see no reason to change our conclusion, when the question before us is a question of depreciation. We have carefully considered the decision of the Third Circuit in *Pittsburgh Brewing Co. v. Commissioner*, 3 Cir. 107 F. 2d 155; but we regard the authority of that decision as greatly weakened by the Third Circuit's decision in *Commissioner v. United States and International Securities Corporation*, 3 Cir. 130 F. 2d 894, which reached the same conclusion that we reached in the *State-Planters Bank & Trust Co. case*.

[fols. 59-60] The method used by the Commissioner for computing depreciation through the remaining years of useful life of the property seems to involve hardship in view of the fact that the taxpayer has received but little tax benefit for the depreciation allowed, and the rates for the remainder of the useful life are less than they would have been if the rates and useful life had been correctly computed in the first instance. The answer is that the remedy is with Congress and not the courts or the executive. Deductions to be allowed from gross income are matters resting in the discretion of Congress; and Congress has expressly provided that the base for computing profits or depreciation must be arrived at by excluding depreciation allowed. The method of spreading the remaining value of the property over the remaining years of useful life is one which has been followed by the Commissioner for many years, and the regulation prescribing it has the effect of law. The pertinent portion of that regulation, Art. 205 of Regulations 77 and 74, is as follows: "The deduction for depreciation in respect of any depreciable property for any taxable year shall be limited to such ratable amount as may reasonably be considered necessary to recover during the remaining useful life of the property the unrecovered cost or other basis."

For the reasons stated, the decision will be reversed and the cause will be remanded for further proceedings not inconsistent herewith.

*Reversed.*



[fol. 61] IN UNITED STATES CIRCUIT COURT OF APPEALS,  
FOURTH CIRCUIT

No. 5004

GUY T. HELVERING, Commissioner of Internal Revenue,  
Petitioner,

VS.

VIRGINIAN HOTEL CORPORATION OF LYNCHBURG, Respondent

On Petition to Review the Decision of The Tax Court of  
the United States, Formerly the United States Board of  
Tax Appeals

JUDGMENT—Filed and Entered January 2, 1943

This Cause came on to be heard on the transcript of the record from The Tax Court of the United States, formerly the United States Board of Tax Appeals, and was argued by counsel.

On Consideration Whereof, It is now here ordered and adjudged by this Court that the decision of the said The Tax Court of the United States, formerly Board of Tax Appeals, in this cause, be, and the same is hereby, reversed; and that this cause be, and the same is hereby, remanded to The Tax Court of the United States for further proceedings in accordance with the opinion of the Court filed herein.

John J. Parker, Senior Circuit Judge. Morris A.  
[fol. 62] Soper, U. S. Circuit Judge. W. Calvin  
Chesnut, U. S. District Judge.

January 27, 1943, petition of respondent for a stay of the mandate pending application for a writ of certiorari is filed.

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IN UNITED STATES CIRCUIT COURT OF APPEALS

ORDER STAYING MANDATE—Filed January 29, 1943

Upon the Application of the Respondent, by its counsel, Frank G. Davidson, Jr., Esq., and for good cause shown,

It Is Ordered that the mandate of this Court in the above entitled cause be, and the same is hereby, stayed pending the application of the said Respondent in the Supreme Court

of the United States for a writ of certiorari to this Court, unless otherwise ordered by this or the said Supreme Court, and provided said application is filed in the said Supreme Court within 30 days from this date.

January 28, 1943.

John J. Parker, Senior Circuit Judge.

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[fol. 63] Clerk's certificate to foregoing transcript omitted in printing.

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[fol. 64] SUPREME COURT OF THE UNITED STATES, OCTOBER TERM, 1942

No. 766

ORDER ALLOWING CERTIORARI—Filed April 5, 1943

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Fourth Circuit is granted, and the case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

(5771)